

EXTRATERRITORIALITY EFFECT OF THE CSDDD ON NON-EU COMPANIES

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ABSTRACT

The Corporate Sustainability Due Diligence Directive (CSDDD) was adopted in June 2024 with the objective of establishing high standards of sustainable business conduct both within the EU and globally. The CSDDD imposes a duty of due diligence on companies for their operations and those of their subsidiaries and other direct or indirect business partners throughout their chains of activities. It is anticipated that the Directive will affect numerous companies doing business in the EU internal market, extending its reach to many non-EU companies and business partners, ranging from large public companies to SMEs and even natural persons. The paper examines the aims and provisions of the CSDDD, focusing on the extension of its impact on non-EU companies. It elaborates on the immediate effects and requirements for companies outside the EU that fall directly within the scope of the Directive and for those covered by its provisions as subsidiaries and business partners in chains of activities. Its main goal is to demonstrate the benefits of extraterritoriality, as well as to examine whether undesirable outcomes could be linked to the extraterritorial effect of the CSDDD.

Key words: sustainability, CSDDD, extraterritorial effect, non-EU Companies, subsidiaries.

1. INTRODUCTION

In May 2024, the EU Council approved the agreement on the Corporate Sustainability Due Diligence Directive (CSDDD), the EU's most ambitious project in the area of corporate sustainability.¹ The first Proposal for the Corporate

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¹ Directive (EU) 2024/1760 of the European Parliament and of the Council of 13 June 2024 on corporate sustainability due diligence and amending Directive (EU) 2019/1937 and Regulation (EU) 2023/2859, (OJ L 2024/1760, 5/7/2024).

Sustainability Due Diligence Directive was made in February 2022, and it took more than two years to be approved by the Council after reaching a political agreement in this important but sensitive area of companies' operations.² Adoption of the CSDDD ended the long, stormy and, at times, the uncertain outcome of the project regarding corporate sustainability due diligence. There is no doubt that this is a multifaceted legislation that will have far-reaching consequences.

The CSDDD aims to impose high standards of business conduct both within the EU and globally. The directive has extremely valuable goals that should be reflected in the more responsible, long-term, sustainable operations of companies. It defines the due diligence duty and establishes a link with the standards of conduct due to the violation of which the Directive foresees a variety of possible sanctions. They include administrative sanctions and civil liability for damage to the injured parties – victims of human rights violations or environmental adverse impacts. Apart from EU companies that are directly covered by the provisions of this Directive – larger companies with a significant number of employees and net turnover – its indirect effect is much wider.

The paper examines the aims and provisions of the CSDDD, focusing on its extraterritorial reach to non-EU companies. It elaborates on the immediate effects and requirements for companies outside the EU that fall directly within the scope of the Directive. It also presents effects on those businesses that are covered by the CSDDD provisions as subsidiaries and business partners in chains of activities.

2. EXTRATERRITORIALITY OF EU LAW

The CSDDD contains provisions that either have extraterritorial application or are affecting directly or indirectly natural or legal persons outside the EU. In general, the extraterritorial application of EU law is not a novelty of the CSDDD and was already recognised on numerous occasions in the EU legal system.³

² Proposal for a Directive of the European Parliament and of the Council on Corporate Sustainability Due Diligence and amending Directive (EU) 2019/1937, COM/2022/71 final, Brussels, 23.02.2022 (further referred to as Proposal for the CSDDD 2022).

³ One of the most recent provisions relates to the Art. 3(2) of the territorial scope of the Regulation (EU) 2016/679 of the European Parliament and of the Council of 27 April 2016 on the protection of natural persons concerning the processing of personal data and on the free movement of such data, and repealing Directive 95/46/EC (General Data Protection Regulation), (OJ L 119, 4/5/2016).

Various terms and notions are used in the literature to explain the extraterritorial effect: the most common is a referral to the *extraterritorial application* or *extraterritorial reach* of the EU law.⁴ Some theoretical works refer to the term or notion of ‘*the Brussels effect*’, based upon works such as the one of Anu Bradford – which points out the legal and political influence of the EU and its legal system on global markets.⁵ Also, the term *trans (EU) territoriality* refers to territory beyond the one consisting of the entirety of EU Member States’ territories, which could be relevant for certain legal issues and the territorial scope of the EU law.⁶

Extraterritoriality usually refers to *territorial extension* – which is considered to exist by the use of territorial connection with the EU to influence conduct that takes place outside the EU.⁷ *Extraterritorial application or reach* of the EU law exists when EU law applies without connection to the EU and beyond its territorial scope.⁸ It is triggered upon various circumstances, including nationality, presence, conduct, effects, anti-evasion, counterparty, or property.⁹ The main objective of this extraterritorial application is usually motivated by EU internal goals, including competition, consumer, or privacy protection.¹⁰ Still, extraterritoriality might be motivated by objectives that are not related to the EU but are internationally accepted universal principles.¹¹ In this case, it is expected to gain more support and global approval. Irrespective of the policy

⁴ Cremona M., Scott, J.: Introduction: EU Law Beyond EU Borders, in: Marise, M., Scott, J. (eds.), *EU Law Beyond EU Borders: The Extraterritorial Reach of EU Law*, Oxford: Oxford University Press, 2019; Scott, J.: The New EU ‘Extraterritoriality’, *Common Market Law Review*, 51(5) 2014; Hornkohl, L.: The Extraterritorial Application of Statutes and Regulations in EU Law, *Max Planck Institute Luxembourg for Procedural Law Research Paper Series*, (1) 2022.

⁵ Bradford, A.: *The Brussels Effect: How the European Union Rules the World*, New York: Oxford University Press, 2020, p. xiv.

⁶ Müller, A. Th.: EWR – Recht und Extraterritorialität, *Liechtensteinische Juristen-Zeitung*, 41(1) 2020, p. 92; Hornkohl, L., The Extraterritorial Application of Statutes and Regulations in EU Law, *Max Planck Institute Luxembourg for Procedural Law Research Paper Series* (1) 2022, p. 4.

⁷ Scott, J.: The New EU ‘Extraterritoriality’, *Common Market Law Review*, 51(5) 2014, p. 1343.

⁸ Hornkohl, L.: The Extraterritorial Application of Statutes and Regulations in EU Law, *Max Planck Institute Luxembourg for Procedural Law Research Paper Series*, (1) 2022, p. 3.

⁹ *Ibid.*, pp. 3, 14-24. See Scott, J.: The New EU ‘Extraterritoriality’, *Common Market Law Review*, 51(5) 2014, pp. 1344, 1348-1363; Chambers, R., Birchall, D.: How European Human Rights Law Will Reshape U.S. Business, *UC Law Business Journal*, 20(1) 2024, p. 22.

¹⁰ Hornkohl, L.: The Extraterritorial Application of Statutes and Regulations in EU Law, *Max Planck Institute Luxembourg for Procedural Law Research Paper Series*, (1) 2022, p. 6.

¹¹ *Ibid.*

objectives, extraterritoriality can always set in motion reciprocal measures of other jurisdictions and result in conflicting rights and obligations, as well as problems of ‘enforcement jurisdiction’.¹² Therefore, it must be carefully evaluated if prescribed.

The most important policy objectives of the CSDDD extraterritoriality are, in the first place, reflected in the protection of universal principles and norms related to sustainability. They are rooted in internationally accepted standards and soft law instruments, which gives them particular significance in their imposition on a global level through their mandatory (and extraterritorial) provisions.¹³ Still, the CSDDD extraterritoriality also remains related to the fulfilment of EU internal goals in creating a level playing field in the EU internal market.

The CSDDD has extraterritoriality effects on numerous points.¹⁴ First, according to its scope, provisions are directly applicable to EU as well as non-EU companies, which are regulated by the law of the third country if certain criteria are met. Also, provisions of the CSDDD imposing due diligence duties affect subsidiaries or business partners in third countries if they are linked to EU companies through chains of activities. Unlike the previous case, where EU law is applied to non-EU companies, in this second case, non-EU companies are affected by the EU law, even though they are not directly included in its scope. These two issues will be further elaborated on in this paper. Apart from that, the CSDDD raises other issues of extraterritoriality regarding substantive and procedural aspects of civil liability imposed on EU and non-EU companies when the damage occurred in third countries and/or human rights breach victims or persons being affected by environmental harm is from outside the EU.¹⁵ These issues will not be further analysed here.

¹² Kuyper, P. J.: European Community Law and Extraterritoriality: Some Trends and New Developments, *The International and Comparative Law Quarterly*, 33(4) 1984, p. 1014; Müller, A. Th.: EWR – Recht und Extraterritorialität, *Liechtensteinische Juristen-Zeitung*, 41(1) 2020, p. 95.

¹³ On this „taking over“ of norms from international law, including soft law see Cremona, M., Scott, J.: Introduction: EU Law Beyond EU Borders, in: Cremona, M., Scott, J. (eds.): *EU Law Beyond EU Borders: The Extraterritorial Reach of EU Law*, Oxford: Oxford University Press, 2019, p. 9.

¹⁴ On some of these points see Enriques, L., Gatti, M.: The Extraterritorial Impact of the Proposed EU Directive on Corporate Sustainability Due Diligence: Why Corporate America Should Pay Attention, University of Oxford Faculty of Law Blogs.

¹⁵ See, for example, on these points Bošković, O.: Extraterritoriality and the proposed directive on corporate sustainability due diligence, a recap, *Journal of Private International Law*, 20(1) 2024, p. 117. See also Perrone, N.: Perspectives of Extraterritorial Jurisdiction for Environmental Damage in the Proposal of the European Directive on Corporate Sustainability Due

3. CORPORATE SUSTAINABILITY DUE DILIGENCE

The CSDDD establishes corporate sustainability due diligence – obligations for companies concerning actual or potential adverse human rights and environmental adverse impacts, both in the operations of the company itself and its subsidiaries and concerning operations of all business partners in the chains of activities.¹⁶ There is also an obligation to combat climate change for companies covered by the provisions of the Directive.¹⁷ It requires companies to adopt and start implementing a climate plan, which will strive to move to climate-neutral business models and strategies following the Paris Agreement 2050 and other provisions in the field of environment, especially climate change law.¹⁸ The CSDDD has enumerated a closed list of international treaties, standards, and other instruments to which due diligence duties are related.¹⁹

Corporate sustainability due diligence is a complex duty, the basic content of which is to conduct risk-based due diligence in (potential – possible or actual) violation of human rights or undesirable environmental impacts. It is an obligation of means and imposes on companies a duty to take appropriate measures to effectively address negative and undesirable consequences of their activities or their business partners.²⁰ Those measures need to be adequately set – in terms of corresponding to risks and possibilities of their negative outcomes.

The due diligence duty is broadly defined and includes various actions not only by the impact of the company's activities but also those performed by its subsidiaries and other business partners in chains of activities. Based on the OECD Guidelines regarding due diligence steps, the CSDDD enumerates the most important actions through which due diligence is to be performed.²¹

Diligence, *The Italian Review of International and Comparative Law*, 3(2) 2023, pp. 403–408; Hornkohl, L.: The Extraterritorial Application of Statutes and Regulations in EU Law, *Max Planck Institute Luxembourg for Procedural Law Research Paper Series*, (1) 2022, pp. 9–13.

¹⁶ Art. 5-16 CSDDD.

¹⁷ Art. 22 CSDDD.

¹⁸ See Art. 1 Para. 1 CSDDD.

¹⁹ Annex to the CSDDD, in which Part I enumerates Rights and Prohibitions Included in International Human Rights Instruments and Human Rights and Fundamental Freedoms Instruments. At the same time, Part II consists of Prohibitions and Obligations included in Environmental Instruments. Critically on the closed list enumeration and with emphasis on possible discrepancies in application of other provisions see: Cantú, R. H.: The Corporate Sustainability Due Diligence Directive beyond Europe, *Verfassungsblog on Matters Constitutional*, 16.06.2024.

²⁰ Recital 19 CSDDD.

²¹ See in detail Recital 20, Art. 7–16 CSDDD, as well as the OECD MNE Guidelines, General Policies, points 11–13.

They include 1) integration of due diligence into management risks and policies, 2) identification, assessment, and prioritisation of actual or potential risks, 3) prevention or mitigation of *potential* and bringing to an end or minimising *existing* adverse impacts and their *remediation*, 4) engagement with stakeholders, 5) establishment of notification and complaints procedure, 6) monitoring of the effectiveness of measures and 7) public communication.

Therefore, due diligence duty consists not only of the implementation of policies and risk management but requires further positive steps in the prevention and cessation of negative impacts of business conduct. Finally, in case of violation of due diligence duty, administrative, legal control and sanctions are provided. It is also possible to compensate damages in case of intent or negligence towards third parties – tort victims for violation of human rights or environmental adverse impacts.

4. LEGAL AND POLITICAL OBJECTIVES OF THE EXTRATERRITORIAL APPLICATION OF THE CSDDD

The basic idea that pervades all the provisions of the CSDDD is the *improvement of business standards and the establishment of sustainable business conduct of companies on a global level* – from the EU, including their subsidiaries and business partners, and outside the borders of the EU. In this way, the EU tries to promote and further develop the principles and standards of sustainable business conduct, starting from those internationally recognised and adopted in the UN Guiding Principles on Business and Human Rights (UN Guiding Principles) and the OECD Guidelines for Multinational Enterprises (MNE Guidelines).²² Better living conditions for all EU citizens and non-EU citizens, easier access to courts, and the protection of their basic rights represent the most valuable legal and political goal, which the intricate provisions of this Directive aim to achieve. The CSDDD should establish a harmonised system of rules and eliminate the inequality of existing (national) rules in this area. Its scope, therefore, goes beyond the EU and is addressed to all companies that actively participate in the internal market that should contribute to global sustainable development and transition.²³

In the introductory part of the CSDDD, the desire of the European Union to contribute to the strengthening of the sustainable economic, social, and environmental development of developing countries on the international stage

²² UN Guiding Principles on Business and Human Rights 2011, OECD: *Guidelines for Multinational Enterprises on Responsible Business Conduct*, Paris: OECD Publishing, 2023, Recital 14 CSDDD.

²³ Recital 16 CSDDD.

is already highlighted in the first recital. The directive is based on the basic values and goals defined in the European Green Deal, a Strong Social Europe for Just Transitions and Communication on decent work worldwide.²⁴ It strives to include especially companies and their business partners in global value chains in the realisation of these agendas.

While trying to impose obligations regarding due diligence in human rights and environmental issues, as well as climate-neutral business conduct, as wide as possible, the CSDDD applies to both EU and non-EU businesses, provided that they conduct their business activities within the EU. There are no further political or legal goals for this extension apart from the general aim to fully achieve the objectives of the Directive.²⁵ Relevant turnover of non-EU companies on the territory of the Union indirectly refers to their **presence on the internal market**, and it is considered to be justifiable to extend the application of the CSDDD to these companies.²⁶

When it comes to the extraterritorial application of the CSDDD provisions, it should also protect EU companies from the **unfair competition** of non-EU companies by imposing the same obligations to all participants on the internal market. Many EU companies fear that they would be at a competitive disadvantage to all other non-EU companies to which due diligence is imposed, particularly when they participate in the EU internal market.²⁷

The effects of extraterritorial application should have an **impact on the global level**, encouraging the acceptance of higher standards in sustainable business and responsible business practices of companies and their business partners all over the world. The European Commission tried to impose due diligence duties on non-EU companies not only for their impact on the internal market but also for their capacity to implement due diligence and benefit from the advantages of that duty.²⁸

²⁴ European Commission: Communication from the Commission to the European Parliament, the European Council, the Council, the European Economic and Social Committee and the Committee of the Regions – The European Green Deal (COM/2019/640 final), 11.12.2019; European Commission: Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions – A Strong Social Europe for Just Transitions (COM/2020/14 final), 14.01.2020; European Commission: Communication from the Commission to the European Parliament, the Council and the European Economic and Social Committee on decent work worldwide for a global just transition and a sustainable recovery (COM/2022/66 final), 23.02.2022.

²⁵ Recital 29 CSDDD.

²⁶ Recital 30 CSDDD.

²⁷ Proposal for the CSDDD 2022, p. 19.

²⁸ Proposal for the CSDDD 2022, p. 16.

5. SCOPE OF THE CSDDD

Corporate sustainability due diligence applies to large EU companies – those which are formed according to the law of the EU Member States.²⁹ Instead of companies with more than 500 employees and net worldwide turnover of more than €150 million (or more than 250 employees and net worldwide turnover of more than €40 million in certain high-impact sectors) as originally proposed, *all companies with more than 1000 employees and with a net turnover of more than €450 million generated worldwide* will be covered. The provisions will initially be applied only to companies with more than 5,000 employees and an income of more than €1.5 billion. Subsequently, in the second phase, the scope will be expanded to include companies with more than 3,000 employees and an income of more than €900 million. Finally, the third phase will embrace all companies falling within the scope of the Directive. CSDDD is also applicable to those companies if they are the ultimate parent companies of a group that had reached this threshold or to other contractual arrangements of franchising or licensing for companies or ultimate parent companies when royalties amounted to a sum greater than €22,5 million and with a net turnover of over €80 million worldwide.

Non-EU companies – CSDDD is also applicable to non-EU companies – those formed according to the law of a third (non-EU) country when they perform significant activities within the EU and irrespective of the number of their employees.³⁰ It includes those non-EU companies (or the ultimate parent company of a group) that have reached the threshold of net turnover of €450 million within the EU. It is also applicable to non-EU companies or ultimate parent companies if royalties for franchising or licencing agreements amount to more than €22,5 million and with a net turnover of over €80 million in the Union. When explaining the reason for imposing such an obligation to non-EU companies, the Proposal for the CSDDD emphasised the *impact on the effects* of the non-EU companies *on the EU internal market*.³¹ In other words, extraterritoriality is explained by the internal goals of the EU related to the level playing field in the EU internal market.

²⁹ For the scope see Art. 2 CSDDD.

³⁰ The Directive explanation was that the threshold regarding employees would be hard to apply to non-EU companies and would lead to legal uncertainties. See Recital 30 CSDDD.

³¹ “The EU turnover criterion for third-country companies creates a link to the EU. Including only turnover generated in the Union is justified since such a threshold, appropriately calibrated, creates a territorial connection between the third-country companies and the Union by the effects that the activities of these companies may have on the EU internal market, which is sufficient for the Union law to apply to third-country companies.” Proposal for the CSDDD 2022, p. 15.

The most important feature of a non-EU company is its presence within the internal market and a certain threshold of net turnover within the EU. Other circumstances, including the nationality of the company, its place of registration, real seat, or other establishment within the EU, are irrelevant.³² The non-EU company need not have even a branch on the territory of the EU for the CSDDD to be applicable.

The CSDDD represents the first general horizontal directive, which includes large companies and their business partners from chains of activities in the EU and third (non-EU) countries. The reasoning behind the provision on the applicability of the CSDDD to large companies is based on the principle of proportionality. The due diligence duty affects only large companies, so obligations imposed with this Directive will not be too burdensome for them. This is due not only to their size but also to their already applicable due diligence policies and mechanisms (for example, from the sustainability reporting requirements that they already have upon existing legislation).³³ Also, large companies are the most prominent players in the internal market with the largest impact on the Union economy.³⁴ Nevertheless, after several changes that followed in the political negotiations and the effort to reach a compromise, there is a relatively small number of EU companies that are directly affected by the provisions of the Directive. According to the initial proposal threshold, it was envisaged to cover approximately 13000 EU and only 4000 non-EU companies. Today, it is estimated that the CSDDD will directly apply to not more than 6000 EU and 900 non-EU companies.³⁵

The CSDDD is compatible with other EU legislation of a general nature (particularly regarding sustainability reporting), as well as specific legislation in

³² Enriques, L., Gatti, M.: The Extraterritorial Impact of the Proposed EU Directive on Corporate Sustainability Due Diligence: Why Corporate America Should Pay Attention, *University of Oxford Faculty of Law Blogs*, 21.04.2024.

³³ The most important provisions in regard to sustainable reporting were regulated by Directive 2014/95/EU of the European Parliament and of the Council of 22 October 2014 amending Directive 2013/34/EU as regards disclosure of non-financial and diversity information by certain large undertakings and groups Text with EEA relevance, (OJ L 330, 15/11/2014) (further referred to as NFRD), later amended by Directive (EU) 2022/2464 of the European Parliament and of the Council of 14 December 2022 amending Regulation (EU) No. 537/2014, Directive 2004/109/EC, Directive 2006/43/EC and Directive 2013/34/EU, as regards corporate sustainability reporting (Text with EEA relevance), (OJ L 322, 16/12/2022) (further referred to as CSRD). CSRD provision will be applied for the first time for 2024 financial year, for reports published in 2025.

³⁴ Proposal for the CSDDD 2022, p. 14–15.

³⁵ European Commission: Directive on Corporate Sustainability Due Diligence: Frequently asked questions, pp. 6-7.

various high-risk sectors of activities. It is worthwhile to remember that corporate sustainability due diligence legislation is complementary to sustainability reporting requirements and that both sets of provisions are addressed to the EU and non-EU companies (if certain threshold conditions are fulfilled).³⁶ Therefore, it is not only that non-EU companies are required to perform corporate sustainability due diligence but are also obliged to report on sustainability issues when performing substantial business activities on the EU internal market.³⁷

6. EXTRATERRITORIAL APPLICATION OF THE CSDDD TO NON-EU COMPANIES

From the extensive personal scope of the CSDDD, it is evident that provisions apply to non-EU companies if they are reaching the threshold of net turnover on the EU internal market. As already underlined, the CSDDD provisions apply to companies (or ultimate parent company of a group) formed in accordance with the law of a third (non-EU) country when they perform significant activities within the EU (when reaching the threshold of net turnover of €450 million in the EU) and irrespective of their number of employees. If that is the case, the law of the Member State of the non-EU company's branch or the place where the highest net turnover was generated will be competent to regulate issues covered by Directive provisions and will be subjected to the supervisory authority of that Member State.³⁸

Non-EU companies have to mandate an authorised representative – a natural or legal person residing or with an establishment in the EU, acting on behalf of the company to comply with obligations regarding sustainability due diligence.³⁹ The obligations of non-EU companies are identical to those of EU companies but include additional communication that, apart from the annual statement, includes information on the authorised EU representative of the company.⁴⁰ Even though this was prescribed to link non-EU companies and the EU, some fear that it is dubious whether these authorised representatives will be able to impose requirements of the directive and assure their applicability

³⁶ Still, during September there were 17 Member States who failed to implement CSRD on time. See for Germany: Stehl, K.: With CSRD and CSDDD Fast Approaching, Germany Keeps Wrangling Over Sustainability Reporting and Supply Chain Due Diligence, University of Oxford Faculty of Law Blogs, 01.11.2024.

³⁷ On the reporting requirements of non-EU companies see Chapter 9a CSRD.

³⁸ Art. 2(7) and Art. 24(3) CSDDD.

³⁹ Art. 3(1) point (k) and Art. 23 CSDDD.

⁴⁰ Art. 16(1) CSDDD.

in non-EU countries and with non-EU companies.⁴¹ Also, it is not clear what the position of the authorised representative is and what sanctions or liability issues can be raised against them.

Finally, the non-EU companies (if falling under the scope of the Directive) will be under the EU supervisory authorities regarding their sustainability duties, who are authorised to impose administrative injunctions and sanctions, including pecuniary ones (fines). This public enforcement can be of primary concern to non-EU companies, particularly when existing national provisions where they operate are less stringent compared to the CSDDD requirements.⁴² While the European Commission expects that this will have a positive impact on foreign business partners through the adoption and implementation of high international standards in their sustainable business conduct and support from EU businesses, it remains to be seen if this is an over-optimistic vision.⁴³

7. NON-EU PARENT COMPANIES, SUBSIDIARIES, OR BUSINESS PARTNERS

The due diligence duty is imposed on large companies (above a certain threshold) for their activities, activities of its subsidiaries, as well as all business partners in chains of activities. Therefore, due diligence obligations also affect the business activities of its subsidiaries and business partners, for whose conduct companies falling under the CSDDD scope are accountable. Also, parent companies, which are non-EU companies, might be affected if their subsidiary falls within the scope of the CSDDD.⁴⁴

⁴¹ Knapp, V.: Proposed EU Directive on Corporate Sustainability Due Diligence: Why Non-EU Businesses Should Respond to the Consultation, *University of Oxford Faculty of Law Blogs*, 18.05.2022; Conac, P. H.: Sustainable Corporate Governance in the EU: Reasonable Global Ambitions?, *RED*, 4(1) 2022, p. 116.

⁴² On the issue of public and private enforcement of the CSDDD provisions see Boschiero, N.: L'extraterritorialità della futura direttiva europea sul dovere di diligenza delle imprese ai fini della sostenibilità, tra diritto internazionale pubblico e privato, *Diritti umani e diritto internazionale*, 17(3) 2023, p. 663.

⁴³ On the European Commission position in that regard see: European Commission: Directive on Corporate Sustainability Due Diligence: Frequently asked questions, 25.07.2024, p. 17.

⁴⁴ It can happen not only through a chain of activities but can also have wide-reaching effects in some national jurisdictions. An example can be taken from the US, including the duty of oversight with liability implications established in the *Caremark* case. See further on the topic: Enriques, L., Gatti, M.: The Extraterritorial Impact of the Proposed EU Directive on Corporate Sustainability Due Diligence: Why Corporate America Should Pay Attention, *University of Oxford Faculty of Law Blogs*, 21.04.2024.

While the CSDDD does not define subsidiaries, it does refer to the general notion of a subsidiary or controlled undertaking as defined in the Accounting and Transparency Directive. For the purposes of this Directive, the term ‘business partner’ encompasses all direct and indirect commercial partners with whom business operations, products, or services are related.⁴⁵ These undertakings can be connected as business partners in the upstream (production of goods or provision of services) or downstream (distribution, transport, and storage) chain of activities. Unlike the scope of the CSDDD provisions, which refer to certain EU and non-EU large companies, there are no other requirements concerning the size or nationality of subsidiaries or business partners in chains of activities. They could, therefore, affect not only large but also SMEs, both from and outside of the EU.

An important drawback of this position is the applicability of multiple codes to non-EU business partners when they are involved in more than one chain of activities.⁴⁶ It can be additionally burdensome if their EU business partners are not from one EU Member State. Therefore, non-EU companies might be compelled to consider international standards and follow obligatory provisions from the CSDDD with additional national provisions of their EU business partners, even though none of them are imposed on them in their national law. Extraterritorial application of the CSDDD to non-EU companies, as well as its indirect effect on them as subsidiaries or business partners, was considered during the preparation of the CSDDD provisions to have positive effects. The most straightforward one is that all business partners of large EU companies will have to ‘adapt’ to EU standards.⁴⁷

Nevertheless, even at that time, there were opinions that this could have the most negative impact in non-EU countries with low standards in human rights and social and environmental protection. In these circumstances, EU

⁴⁵ Art. 3(1), points (e) (f) and (g) CSDDD in regard to Article 2, point (10), of Directive 2013/34/EU and Article 2(1), point (f), of Directive 2004/109/EC (Directive 2013/34/EU of the European Parliament and of the Council of 26 June 2013 on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings, amending Directive 2006/43/EC of the European Parliament and of the Council and repealing Council Directives 78/660/EEC and 83/349/EEC Text with EEA relevance, (OJ L 182, 29/06/2013) and Directive 2004/109/EC of the European Parliament and of the Council of 15 December 2004 on the harmonisation of transparency requirements in relation to information about issuers whose securities are admitted to trading on a regulated market and amending Directive 2001/34/EC, (OJ L 390, 31/12/2004).

⁴⁶ Conac, P. H.: Sustainable Corporate Governance in the EU: Reasonable Global Ambitions?, *RED*, 4(1) 2022, p. 116.

⁴⁷ Enriques, L., Gatti, M.: The Extraterritorial Impact of the Proposed EU Directive on Corporate Sustainability Due Diligence: Why Corporate America Should Pay Attention, *University of Oxford Faculty of Law Blogs*, 21.04.2024.

companies have the possibility of temporarily suspending or terminating business operations or connections with business partners from these countries, which might, for many of them, have negative effects.⁴⁸ Another potential risk in the involvement of numerous business partners in chains of activities could be in the reduction of contractual partners with other negative effects in third countries, including less diversified investments, monopolisation, and lower efficiency.⁴⁹ Being of utmost importance to the extraterritorial effect, we will further elaborate on these challenges.

8. CHALLENGES

So far, everyone agrees on one thing: the goals that the CSDDD promotes and wants to achieve are extremely important and not generally disputable. However, there are many different and even contradictory views on how the Directive envisaged their achievement.

8.1. CHALLENGES FOR EU COMPANIES

The usual criticism of the CSDDD starts with the inefficient legal framework that essentially does not achieve its legal and political goals.⁵⁰ Today, it is evident that even some EU Member States, such as Germany, are considering postponing the CSRD application and renegotiating the CSDDD.⁵¹ Predictions by which EU standards in sustainable business could be applied globally are considered unrealistic, which leads to an **uncompetitiveness of European companies** with companies operating in the American or Asian markets.⁵² This is contradictory to the initial aims of EU legislators. Namely, it was precisely the fear of competition that, according to some opinions, led to the imposition of the extraterritorial reach of the CSDDD provisions.⁵³

⁴⁸ Proposal for the CSDDD 2022, p. 19.

⁴⁹ Schmid, S., Thomale, C.: Private Enforcement in the EU Corporate Sustainability Due Diligence Directive-A critical comparative law and economic analysis of the Final Compromise, *University of Oxford Faculty of Law Blogs*, 22.05.2024.

⁵⁰ Schmid, S., Thomale, C.: Gastbeitrag: EU-Lieferkettenrichtlinie: Richtiges Ziel, fraglicher Weg, *Der Standard*, 24.04.2024.

⁵¹ See for Germany in particular: Stehl, K., With CSRD and CSDDD Fast Approaching, Germany Keeps Wrangling Over Sustainability Reporting and Supply Chain Due Diligence, *University of Oxford Faculty of Law Blogs*, 01.11.2024.

⁵² *Ibid.*

⁵³ Conac, P.H.: Sustainable Corporate Governance in the EU: Reasonable Global Ambitions?, *RED*, 4(1) 2022, p. 117.

Further, there are no problems from a strategic point with imports of materials into the EU originating from developed countries (like imports of raw materials having the highest share of imports from the U.S. 12%, Canada 7.2%, etc.).⁵⁴ Still, the EU imports are in some cases strategically dependent on some business partners in more critical countries with lower levels of human rights and environmental protection – like some of these products originating from China (52%) or Vietnam (11%).⁵⁵ In those critical areas, there is not much leverage with change in practices and policies, bearing in mind the limited nature of resources or materials.⁵⁶ There is a risk that the only viable option could be **disengagement with business partners** from these countries or with high-risk potential, even though the CSDDD is focused on not letting this happen if there are other options available. It promotes engagement with business partners through mitigation of adverse impacts and is, according to the European Commission, going to have long-term positive impacts.⁵⁷ It is, therefore, expected that the CSDDD will have what is referred to as a ‘trickle-down effect’⁵⁸ – a phenomenon of imposing higher standards (or products) available only to wealthier to the wider public with a decrease of costs and adjustment in affordability. Still, temporary suspension or termination of business contacts might not be an option for those raw materials or resources without alternative business partners.⁵⁹ That could further intensify not only problems of strategic dependency but also other political or social problems and ultimately pose a systemic economic risk for EU companies.⁶⁰ From the other perspective, high standards that might be too excessive to reach in certain developing countries might lead to redirection to other value chains and partners in (more developed) other countries.⁶¹ Already, there have been concerns in many developing

⁵⁴ Commission Staff Working Document, Follow-up to the second opinion of the Regulatory Scrutiny Board Accompanying the document Proposal for a Directive of the European Parliament and of the Council on Corporate Sustainability Due Diligence and amending Directive (EU) 2019/1937, SWD(2022)39, 23/02/2022 (further referred to as European Commission, Follow-up), p. 22.

⁵⁵ *Ibid.*

⁵⁶ *Ibid.*

⁵⁷ *Ibid.*, pp. 26–27.

⁵⁸ Mares, R.: The Unintended Consequences of Mandatory Due Diligence: The Importance of Supportive Measures in the EU Corporate Sustainability Due Diligence Directive, *Verfassungsblog on Matters Constitutional*, 13.06.2024.

⁵⁹ Conac, P.H., Sustainable Corporate Governance in the EU: Reasonable Global Ambitions?, *RED*, 4(1) 2022, p. 117.

⁶⁰ *Ibid.*, pp. 117–118.

⁶¹ Mares, R.: The Unintended Consequences of Mandatory Due Diligence: The Importance of Supportive Measures in the EU Corporate Sustainability Due Diligence Directive, *Verfassungsblog on Matters Constitutional*, 13.06.2024.

countries that they would fail to meet these requirements, which would result in their exclusion from the European internal market.⁶²

The usual criticism is that the CSDDD **increases transaction costs**, which could have negative effects on business relationships with partners from undeveloped countries.⁶³ These have already been demonstrated in the economic analysis of the German Law on Supply Chain.⁶⁴ The CSDDD also **increases compliance costs**. Even though the CSDDD requires initial compliance costs for companies, the European Commission has claimed that they should be lower in the long run in comparison to the benefits achieved through its application.⁶⁵ This is particularly the case because, after initial costs for EU companies falling under the scope of the CSDDD, they will have benefits in the long run, including profitability, innovation, reduction of legal and reputational risks, etc. Nevertheless, some argue that compliance with these provisions, in particular of international treaties and standards aimed at states and not companies, could be not only costly but also very difficult to enforce.⁶⁶ The same can be the issue of applying provisions and standards of a general nature to particular business activities. At the end of the day, even if those costs would be significant, large companies within the scope of the CSDDD will be able to bear them with no difficulty.⁶⁷

Finally, some authors find that the CSDDD still represents a **missed opportunity** to impose group liability instead of a liability on the entity level.⁶⁸ It does not eliminate the negative effects of limited liability, particularly by not

⁶² *Ibid.*

⁶³ Schmid, S., Thomale, C.: Private Enforcement in the EU Corporate Sustainability Due Diligence Directive-A critical comparative law and economic analysis of the Final Compromise, *University of Oxford Faculty of Law Blogs*, 22.05.2024.

⁶⁴ Schmid, S., Thomale, C.: Private Enforcement in the EU Corporate Sustainability Due Diligence Directive-A critical comparative law and economic analysis of the Final Compromise, *University of Oxford Faculty of Law Blogs*, 22.05.2024.

⁶⁵ European Commission, Follow-up, pp. 26-27.

⁶⁶ Ferrarini, G.: Corporate Sustainability Due Diligence and the Shifting Balance between Soft Law and Hard Law in the EU, *University of Oxford Faculty of Law Blogs*, 22.04.2022; Conac, P. H.: Sustainable Corporate Governance in the EU: Reasonable Global Ambitions?, *RED*, 4(1) 2022, p. 117.

⁶⁷ With this conclusion in regard to non-EU companies see Chambers, R., Birchall, D.: How European Human Rights Law Will Reshape U.S. Business, *UC Law Business Journal*, 20(1) 2024, p. 52.

⁶⁸ Pargendler, M.: The EU Proposal on Corporate Sustainability Due Diligence and the Mystique of Complete Corporate Separateness, *University of Oxford Faculty of Law Blogs*, 11.04.2022.

imposing parent liability for torts committed by its subsidiaries.⁶⁹ That is particularly challenging from the extraterritoriality perspective, bearing in mind that one of the primary goals of the CSDDD was the global introduction of international standards of sustainable business conduct and the potential liability of (all) in-scope companies for failure to comply with them. Other issues of civil liability, which were not discussed in this paper, such as the extraterritorial jurisdiction and other procedural and substantive private international law issues, also point out possible deficiencies in this regard.⁷⁰ They could call for negative countermeasures in other jurisdictions, imposing reciprocity of extraterritorial treatment.⁷¹

8.2. NON-EU COUNTRIES REACTIONS TO THE CSDDD

Reception of the CSDDD in third countries has so far not been always promising. Many concerns have already been raised, even before the CSDDD becomes applicable. Also, there are concerns about the ‘value-exporting approach’ taken by the CSDDD.⁷² Many think that extraterritorial outreach is not acceptable from the third countries’ perspective, obliging their companies to stringent provisions to which there was no possibility to debate or influence decision-making.⁷³ Also, several other issues were raised, including jurisdiction shopping, symbolical engagement with local communities and business partners, and irresponsible disengagement, among others.⁷⁴

It is not surprising that strong opposition came from the U.S., the leading raw material exporter and one of the most important parts of the world from where

⁶⁹ *Ibid.* Similar conclusions with regard to liability and failure to define burden of proof were also raised by: Paces, A., Supply Chain Liability in the Corporate Sustainability Due Diligence Directive Proposal, *University of Oxford Faculty of Law Blogs*, 20.04.2022.

⁷⁰ On the procedural aspect see, for example, Perrone, N.: Perspectives of Extraterritorial Jurisdiction for Environmental Damage in the Proposal of the European Directive on Corporate Sustainability Due Diligence, *The Italian Review of International and Comparative Law*, 3(2) 2023, p. 403; as well as Farah, Y., Kunuji, V., Kent, A.: Civil Liability Under Sustainability Due Diligence Legislation: A Quiet Revolution?, *King’s Law Journal*, 34(3) 2023, pp. 519-522.

⁷¹ See in regard to extraterritorial scope of CSRD, but with same effect to other issues: Conac, P.H., Sustainable Corporate Governance in the EU: Reasonable Global Ambitions?, *RED*, 4(1) 2022, p. 115.

⁷² Bueno, N. et al.: The EU Directive on Corporate Sustainability Due Diligence (CSDDD): The Final Political Compromise, *Business and Human Rights Journal*, 9(2) 2024, p. 5.

⁷³ Hagerty, B.: Barr sound alarm on Europe’s regulatory encroachment: Biden-Harris Administration idles as Europe unleashes far-left policy agenda on American businesses, 27.09.2024.

⁷⁴ McCullagh, V.: The EU Corporate Sustainability Due Diligence Directive: Real Change or More of the Same?, *European Business Law Review*, 35(5) 2024, p. 604.

companies do business on the EU internal market. Preliminary calculations pointed out that an estimation of 3500 U.S. businesses would have been directly affected, while even more would have indirectly had to comply with EU law.⁷⁵ This number is slightly lowered by amendments to the scope of the CSDDD, bearing in mind that the calculation was made upon the initial proposal with the (much larger) scope of companies concerned.

Many reactions in the U.S. media are extremely negative and find the CSDDD product of a 'far-left policy agenda' with 'regulatory encroachment' on American businesses.⁷⁶ The example of the U.S. Prioritizing Economic Growth Over Woke Policies Act, as well as Protecting U.S. Business Sovereignty Act, shows that the U.S. finds the CSDDD provisions regarding non-EU companies 'harmful' to business and the economy.⁷⁷ Other world-leading exporters, including China, are worried about 'increased bureaucracy and the unbalanced, disproportionate and ambiguous obligations imposed on businesses'.⁷⁸

Other non-EU commentators joined in putting forward their concerns about the implementation of practices in their local businesses of 'a legal instrument that they did not adopt, and that is not legally binding in their territories'.⁷⁹ Voices outside the EU underline that there has been a lack of engagement of the EU with those countries where the CSDDD and other similar acts would have the greatest impact.⁸⁰ Therefore, some think that the CSDDD will become a new 'neo-colonial' tool for Western European countries.⁸¹ This is particularly the case because extraterritorial effects come from the home state(s)

⁷⁵ Chambers, R., Birchall, D.: How European Human Rights Law Will Reshape U.S. Business, *UC Law SF Business Journal*, 20(1) 2024, p. 42.

⁷⁶ Hagerty, B.: Barr sound alarm on Europe's regulatory encroachment: Biden-Harris Administration idles as Europe unleashes far-left policy agenda on American businesses, 27.09.2024.

⁷⁷ Meuser Dan, Press Release, 20.09.2024. Further, regarding U.S. companies, see Chambers, R., Birchall, D.: How European Human Rights Law Will Reshape U.S. Business, *UC Law SF Business Journal*, 20(1) 2024, pp. 42-51. See also Enriques, L., Gatti, M.: The Extraterritorial Impact of the Proposed EU Directive on Corporate Sustainability Due Diligence: Why Corporate America Should Pay Attention, *University of Oxford Faculty of Law Blogs*, 21.04.2024.

⁷⁸ Hancock, A., Bounds, A.: EU's new environmental laws irk developing countries, *Financial Times*, 15.03.2024.

⁷⁹ Cantú, R. H.: The Corporate Sustainability Due Diligence Directive beyond Europe, *Verfassungsblog on Matters Constitutional*, 14.06.2024.

⁸⁰ *Ibid.*

⁸¹ See on different perspectives in that regard Symposium – Colonisation in, of and through Business & Human Rights, <<https://www.tilburguniversity.edu/overview/symposium-colonisation-business-human-rights>>, last accessed on 05/11/2024. See also conclusions in Chambers, R., Birchall, D.: How European Human Rights Law Will Reshape U.S. Business, *UC Law SF Business Journal*, 20(1) 2024, p. 51.

of corporations, without proper concern and difficulties of companies, communities, or people from non-EU countries who are affected by these issues existentially.⁸² They are usually without a right to have a voice in the process and are subjected to ‘domination, subordination and serious disadvantage’, even though it is typically where the majority of violations of human rights and adverse environmental impacts take place.⁸³

It has been emphasised on many occasions that the EU must adopt an intense strategy to improve engagement with third countries, make clear what standards and practices are required from business partners, and specify negative effects if they fail to meet them.⁸⁴ Otherwise, many business partners in chains of activities will be faced with too high requirements, which they cannot meet without proper (EU) support. That could place undeveloped countries and their businesses in a weak position while distorting trade and ‘hurting those it claims to protect’.⁸⁵ Still, the burden of compliance exists for non-EU business partners from undeveloped and developed countries.⁸⁶ For some businesses, disengagement would not be that detrimental but would rather be an evaluation of compliance costs against EU internal market involvement.⁸⁷ In any case, the outcome will not always be in accepting the high business standards aimed by the CSDDD’s provisions.

9. CONCLUSION

The CSDDD aims to impose high standards of business conduct both within the EU and globally. There is strong support in favour of high political goals, which are at the bottom of this important document. Nevertheless, there are still many challenges remaining in how to overcome these goals globally, bringing equality and prosperity for all.

⁸² Lichuma, C.O.: (Laws) Made in the ‘First World’: A TWAIL Critique of the Use of Domestic Legislation to Extraterritorially Regulate Global Value Chains, *ZaöRV*, 81(2) 2021, p. 500.

⁸³ *Ibid.*, pp. 513, 518.

⁸⁴ Cantú, R. H., The Corporate Sustainability Due Diligence Directive beyond Europe, *Verfassungsblog on Matters Constitutional*, 14.06.2024.

⁸⁵ Mares, R., The Unintended Consequences of Mandatory Due Diligence: The Importance of Supportive Measures in the EU Corporate Sustainability Due Diligence Directive, *Verfassungsblog on Matters Constitutional*, 13.06.2024.

⁸⁶ Regarding U.S. small firms, see Chambers, R., Birchall, D.: How European Human Rights Law Will Reshape U.S. Business, *UC Law SF Business Journal*, 20(1) 2024, p. 52.

⁸⁷ *Ibid.*

Today, it is evident that even some EU Member States, such as Germany, are considering postponing the CSRD application and renegotiating the CSDDD. Non-EU countries that have high political influence might do the same. Underdeveloped countries are afraid that they will be banned from the EU internal market by failing to reach high standards of their business conduct in a short period.

Forthcoming business conduct imposed by the CSDDD must be scrutinised and evaluated once this important legislation becomes effective. Hopefully, most European as well as non-EU businesses will seek to enhance research, innovation, and imposition of more sustainable business conduct. However, various challenges remain. Above all, it would be undesirable for companies to try to evade or decide not to apply the mandatory *due diligence* measures imposed by the CSDDD. It is to be hoped that once the CSDDD becomes applicable, many of the challenges will prove to be unsubstantiated or will be resolved. Until then, it is more than ever welcome for the EU to engage with undeveloped countries and to push large in-scope companies to provide support – various protective or supportive measures to their partners in their chains of activities, particularly SMEs. Detailed practices and standards of engagement should be further promoted, developed and insisted upon, and they must prevail over disengagement, involving the most undeveloped business partners in chains of activities above all.

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