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WHAT DOES THE EU CSDDD SAY ABOUT CONTRACTS?

SARAH DADUSH*, DANIEL SCHÖNFELDER**, & MICHAELA STREIBELT***

* Sarah Dadush, Professor of Law & Founding Director, the Responsible Contracting Project (RCP), Rutgers Law School.
** Daniel Schönfelder, Lead European Legal Advisor, RCP.
*** Michaela Streibelt, European Legal Advisor, RCP.

Introduction

After years of contentious negotiations, the European Union (EU) Corporate Sustainability Due Diligence Directive (CSDDD) entered into force in July 2024.[1] The CSDDD (hereinafter used interchangeably with "the Directive") can fairly be described as the most significant piece of legislation pertaining to corporate social and environmental performance in existence. As far as its scope, the Directive will eventually apply to EU companies with more than 1,000 employees[2] with an annual global turnover exceeding EUR 450 million. It will also apply to non-EU companies with an annual turnover of EUR 450 million in the EU.[3] There is no worker threshold for non-EU companies.[4] It will also apply to EU and non-EU "ultimate parent companies" of groups of EU and non-EU companies that, taken together as a group, meet the revenue and worker thresholds above.[5] On timing, the largest of the in-scope companies must be compliant by 2027, the next largest by 2028, and the last by 2029.[6]

With respect to substantive requirements, Article 5 ("Due Diligence") requires in-scope companies to identify and assess the actual or potential adverse human rights and environmental (HRE) impacts[7] of their own operations, the operations

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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, 2024 O.J. (L) [hereinafter CSDDD]. As the CSDDD is an EU Directive and not a Regulation, it must be transposed into the national law of each Member State to be enforced. The transposition process is now underway, with some Member States moving a bit faster than others.

2. *Id.* recital 28 (setting out the types (e.g., full-time, part-time, seasonal) of workers who should be counted toward the employee threshold).

3. *Id.* art. 2 (scope).

4. *Id.*

5. *Id.* For analysis of what the CSDDD means for American companies, see Luca Enriques, Matteo Gatti & Roy Shapira, *How the EU Sustainability Due Diligence Directive Could Reshape Corporate America*, 78 Stan. L. Rev. (forthcoming) (Eur. Corp. Governance Inst., Working Paper No. 817/2025, 2025), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=5083571.

6. CSDDD, *supra* note 1, art. 37.

7. Adverse human rights impacts are impacts on persons resulting from the abuse of the human rights enshrined in the international instruments listed in the Annex (Part I) of the CSDDD. These rights include, among others, the right to life; the right to enjoy just and favourable conditions of work, which itself includes a fair wage and an adequate living wage for employed workers and an adequate living income for self-employed workers and smallholders, as well as a decent living, safe and healthy working conditions, and

of their subsidiaries, and the operations of business partners in the in-scope company's "chain of activities."[8] The chain of activities includes the company's upstream business partners (the company's supply chain) and some downstream partners.[9] However, unlike simple disclosure regulations, the CSDDD requirements go beyond mere identification and reporting of HRE risks; companies must, on the basis of their due diligence and risk-assessment process, take affirmative, dynamic, and proactive measures to prevent the escalation of potential adverse impacts to actual adverse impacts.[10] The *prevention* of adverse impacts, effectuated through appropriate risk-mitigation and preventive measures, is therefore a critical aspect of CSDDD compliance.

The Directive doesn't stop at prevention either. It also requires companies that discover adverse impacts through their due diligence to bring such impacts to an end and to take appropriate measures to ensure they do not reoccur. Important for contracts, companies must first seek to address adverse

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reasonable limitations of working hours; the right of the child to be protected from economic exploitation; the prohibition of forced or compulsory labor; the right to freedom of association, assembly, and the rights to organize and collective bargaining; the rights of individuals, groups, and communities to lands and resources and to not be deprived of means of subsistence. *Id.* annex (pt. I). Adverse environmental impact means an adverse impact on the environment resulting from a breach of the prohibitions and obligations listed in the Annex (Part II) of the CSDDD. The Annex does not include climate-related expectations, but these are covered by the obligations under Art. 22 which obliges companies to implement climate adaptation plans *Id.* annex (pt. II), art. 22.

8. The chain of activities covers "activities of a company's upstream business partners related to the production of goods or the provision of services by the company, including the design, extraction, sourcing, manufacture, transport, storage and supply of raw materials, products or parts of the products and development of the product or the service, and activities of a company's downstream business partners related to the distribution, transport and storage of the product, where the business partners carry out those activities for the company or on behalf of the company." The Directive does not cover the disposal of the product. *Id.* recital 25.

9. As concerns carrying out HREDD to manage impacts related to using products, the EU Commission's FAQs on the CSDDD say "[a]s regards the impacts of the products or services through their use, companies in scope are required to identify adverse impacts linked to their own operations, and make the necessary modifications to their business plan, overall strategies and operations, including the design of products/services, purchasing and distribution practices." Eur. Comm'n, Directive on Corporate Sustainability Due Diligence Frequently asked questions, at 10.

10. CSDDD, *supra* note 1, art. 5 (due diligence).

impacts before moving to terminate the business relationship at issue.[11] In other words, exit must not be the first response to an adverse impact, whether potential or actual.[12] Rather, both Articles 10 (Preventing Potential Adverse Impacts) and 11 (Bringing Actual Adverse Impacts to an End) clarify that disengagement from a business relationship, including via contractual termination, must be pursued only as a "last resort", in situations where there is no reasonable expectation that preventive or corrective measures will succeed.[13] Last, but certainly not least, Article 12 (Remediation of Actual Adverse Impacts) requires companies to provide remedy to the persons adversely affected by the impact—the victims—if the company caused or jointly caused the impact.[14] Thus, along with prevention of harm, victim-centered remediation, is another critical aspect of CSDDD compliance.

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11. Article 10(6)(b) and 11(7) state that, as concerns potential adverse impacts that could not be prevented or adequately mitigated by appropriate measures, and as concerns actual adverse impacts that could not be brought to an end, or the extent of which could not be adequately minimised by appropriate measures, "the company shall, as a last resort, be required to refrain from entering into new or extending existing relations with a business partner in connection with which, or in the chain of activities of which, the impact has arisen." Further, if the adverse impact is severe and "there is no reasonable expectation that [preventive or corrective] efforts would succeed," the company "shall, as a last resort, … terminate the business relationship with respect to the activities concerned." *Id.* arts. 10(6)(b), 11(7)(b). As a final potential hurdle to termination, "prior to temporarily suspending or terminating a business relationship, the company shall assess whether the adverse impacts from doing so can be reasonably expected to be manifestly more severe than the adverse impact that could not be prevented or adequately mitigated. Should that be the case, the company shall not be required to suspend or to terminate the business relationship, and shall be in a position to report to the competent supervisory authority about the duly justified reasons for such decision." *Id.* arts. 10(6), 11(7).

12. *Id.* art. 11(7).

13. *Id.* arts. 10(6), 11(7).

14. "'[R]emediation' means restoration of the affected person or persons, communities or environment to a situation equivalent or as close as possible to the situation they would have been in had an actual adverse impact not occurred, in proportion to the company's implication in the adverse impact, including by financial or non-financial compensation provided by the company to a person or persons affected by the actual adverse impact and, where applicable, reimbursement of the costs incurred by public authorities for any necessary remedial measures." *Id.* art. 3 (definitions). Article 12(1) states: "Member States shall ensure that, where a company has caused or jointly caused an actual adverse impact, the company provides remediation." *Id.* art. 12(1).

This holistic approach to managing HRE risks in corporate supply (and value) chains is known as human rights and environmental due diligence (HREDD). It was first set out in the United Nations Guiding Principles on Business and Human Rights (UNGPs),[15] which serve, along with the OECD Guidelines for Multinational Enterprises on Responsible Business Conduct (OECD Guidelines) and the OECD Due Diligence Guidance for Responsible Business Conduct (OECD Guidance),[16] as the building blocks of the CSDDD.[17] While the CSDDD does not directly translate these widely-recognized responsible business conduct standards into hard law, they do and will continue to inform how companies, implementing bodies, civil society, and

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15. The UNGPs were unanimously endorsed by the UN Human Rights Council in 2011. They address the responsibility of governments to protect human rights (Pillar I), the responsibility of companies to respect human rights (Pillar II), and the responsibility of both government and companies to provide remedy to adversely impacted stakeholders (Pillar III). United Nations, Guiding Principles on Business and Human Rights 3 (2011) [hereinafter UNGP], https://www.ohchr.org/sites/default/files/documents/publications/guidingprinciplesbusinesshr_en.pdf; *see also,* John G. Ruggie & John F. Sherman, III, *Adding Human Rights Punch to the New Lex Mercatoria: The Impact of the UN Guiding Principles on Business and Human Rights on Commercial Legal Practice*, 6 J. Int'l Disp. Settlement 455, 456 (2015) (discussing the implications for private commercial legal practice of a company's commitment to respect human rights and to reflect that commitment in its commercial relationships); Sarah Dadush, Daniel Schönfelder & Bettina Braun, *Complying with Mandatory Human Rights Due Diligence Legislation through Shared-Responsibility Contracting: The Example of Germany's Supply Chain Act (LkSG)*, *in* Contracts for Responsible and Sustainable Supply Chains: Model Contract Clauses, Legal Analysis, and Practical Perspectives (Susan Maslow & David Snyder eds., 2023) [hereinafter, Dadush et al., *Complying with Mandatory Human Rights Due Diligence*].

16. Org. for Econ. Coop. and Dev [hereinafter OECD], OECD Guidelines for Multinational Enterprises on Responsible Business Conduct (2023) [hereinafter OECD Guidelines], https://doi.org/10.1787/81f92357-en; OECD, OECD Due Diligence Guidance for Responsible Business Conduct (2018) [hereinafter OECD Guidance], https://mneguidelines.oecd.org/due-diligence-guidance-for-responsible-business-conduct.htm.

17. Recital 20 highlights the close connection between Article 5 (due diligence) and the OECD Guidance: "The due diligence process set out in this Directive should cover the six steps defined by the [OECD] Guidance for Responsible Business Conduct .... That process encompasses the following steps: (1) integrating due diligence into policies and management systems; (2) identifying and assessing adverse human rights and environmental impacts; (3) preventing, ceasing or minimising actual and potential adverse human rights and environmental impacts; (4) monitoring and assessing the effectiveness of measures; (5) communicating and (6) providing remediation." CSDDD, *supra* note 1, recital 20.

other stakeholders interpret the CSDDD, particularly in cases of doubt. Because the CSDDD adopts the HREDD approach to corporate social and environmental responsibility, it is different from disclosure regulation, which has been the focus until now.[18] Disclosure regulation has been criticized for its limited effectiveness because it asks companies only to disclose what they are doing to address HRE matters, without requiring that they actually do those things or holding them accountable if they fail to do those things.[19] The EU's Corporate Sustainability Reporting Directive (CSRD)[20], which went into force in 2023 and replaced the Non-Financial Reporting Directive (NFRD)[21], deals with HRE reporting. On its own, the CSRD would have

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18. *See* Sarah Dadush, *Prosocial Contracts: Making Relational Contracts More Relational*, 85 L. & Contemp. Probs. 153, 168 (2022) [hereinafter Dadush, *Prosocial Contracts*] (explaining that "[b]usinesses must take affirmative measures—appropriate to the severity of the risk at issue—to prevent it from materializing into actual harm" and "risk-identification is not the end of HR[E]DD, but a component of HR[E]DD …. This makes HR[E]DD legislation—which transforms GP17 into hard law—fundamentally different from simple disclosure laws like the California Transparency in Supply Chains Act or the United Kingdom Modern Slavery Act"). UNGP 17 says: 'In order to identify, prevent, mitigate and account for how they address their adverse human rights impacts, business enterprises should carry out human rights due diligence. The process should include assessing actual and potential human rights impacts, *integrating and acting upon the findings, tracking responses, and communicating how impacts are addressed.*'"). UNGP, *supra* note 15, 17.

19. *See* Ruth Green, *UK Modern Slavery Act failings point to need for global action on slavery*, Int'l Bar Ass'n, https://www.ibanet.org/article/57fc8a75-2a33-422c-9274-e98e53056472; UK Modern Slavery Act: Missed opportunities and urgent lessons, Bus. & Hum. Rts. Res. Ctr. (Feb. 25, 2021), https://www.business-humanrights.org/en/from-us/briefings/uk-modern-slavery-act-missed-opportunities-and-urgent-lessons/; Australia's Modern Slavery Act: is it fit for purpose?, Bus. & Hum. Rts. Res. Ctr. (Apr. 3, 2023), https://media.business-humanrights.org/media/documents/Australias_Modern_Slavery_Act.pdf; Kishanthi Parella, *Protecting Third Parties in Contracts*, 58 Am. Bus. L. J. 327, 361–65 (2020) and accompanying footnotes (providing an overview of the weaknesses of disclosure laws); *see also*, Jaakko Salminen & Mikko Rajavuori, *Transnational Sustainability Laws and the Regulation of Global Value Chains: Comparison and a Framework for Analysis*, 26 Maastricht J. Eur. and Compar. L. 602, 627 (2021).

20. Directive 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, 2022 O.J. (L 322) 15.

21. 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, 2014 O.J. (L 330) 1.

done little to move beyond disclosure, but, with the adoption of the CSDDD a year later, the EU regime became the first to really bring due diligence and reporting together, making them work hand in hand to regulate corporate HRE performance.

Although the CSDDD is rigorous, it is critical to understand that it does not expect companies to achieve perfection, but rather to demonstrate continuous improvement. The CSDDD mainly contains "obligations of means," not "obligations of results."[22] Otherwise put, the CSDDD operationalizes a negligence standard of care for assessing HRE performance; it does not create a strict liability regime. As such, it does not outlaw imperfection or the occurrence of adverse impacts, but rather accommodates it as a matter of course. Companies will not run afoul the CSDDD just because they have (or discover) adverse impacts in their chain of activities, but they could be in violation if they fail to establish and maintain appropriate processes to identify,[23] prevent, mitigate, bring to an end, and, as needed, remedy those impacts.

Another important feature of the CSDDD is that, as highlighted above, it applies to (very) large companies wherever they are incorporated or headquartered. So long as they hit the applicable revenue and employee thresholds, the CSDDD requires companies doing business in the EU to conduct HREDD across their supply chains and parts of their value chains. Furthermore, although the CSDDD applies only to large companies, it will have major implications well beyond those companies because due diligence requirements will need

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22. CSDDD, *supra* note 1, recital 19 ("*This Directive should not require companies to guarantee, in all circumstances, that adverse impacts will never occur or that they will be stopped.* For example, with respect to business partners, where the adverse impact results from State intervention, the company might not be in a position to arrive at such results. *Therefore, the main obligations in this Directive should be obligations of means.* The company should *take appropriate measures which are capable of achieving the objectives of due diligence by effectively addressing adverse impacts, in a manner commensurate to the degree of severity and the likelihood of the adverse impact.* Account should be taken of the circumstances of the specific case, the nature and extent of the adverse impact and relevant risk factors, including, in preventing and minimising adverse impacts, the specificities of the company's business operations and its chain of activities, sector or geographical area in which its business partners operate, the company's power to influence its direct and indirect business partners, and whether the company could increase its power of influence.") (emphases added).

23. With respect to identification, Article 5 adds, "where necessary, prioritising actual and potential adverse impacts in accordance with Article 9." *Id.* art. 5.

to be implemented across their own operations, the operations of their subsidiaries, and those of business partners involved in their chain of activities. [24] To be clear, only in-scope companies are legally obligated to adhere to the CSDDD requirements, so when we say that the requirements must be implemented in the operations of subsidiaries and business partners, that does not mean that HREDD responsibilities belong to those entities; rather, the in-scope company is responsible for taking measures, including contractual measures, to improve living and working conditions, which includes environmental protection, across its chain of activities. One should therefore understand the Directive's scope as covering not just individual companies, but also the companies' commercial relationships, which are often mediated through contracts. [25]

Contracts have long been vehicles of choice for companies to implement human rights and environmental standards across their supply chains.[26] As privately negotiated instruments, contracts are flexible and allow companies to set tailored standards

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24. Article 8 on "Identifying and assessing potential and actual adverse impacts" states: "Member States shall ensure that companies take appropriate measures to identify and assess actual and potential adverse impacts arising from their own operations or those of their subsidiaries and, where related to their chains of activities, those of their business partners, in accordance with this Article." *Id.* art. 8. Recital 16 explains that the CSDDD "aims to ensure that companies active in the internal market contribute to sustainable development and the sustainability transition of economies and societies through the identification, and where necessary, prioritisation, prevention and mitigation, bringing to an end, minimisation and remediation of actual or potential adverse human rights and environmental impacts connected with companies' own operations, operations of their subsidiaries and of their business partners in the chains of activities of the companies, and ensuring that those affected by a failure to respect this duty have access to justice and legal remedies." *Id.* art. 16.

25. As explained in the briefing note by the consultancy, Human Level, "[t]he fact that the Directive doesn't apply to as many companies as initially envisioned doesn't matter. A much greater number of companies will be affected by this Directive, by virtue of how the Directive's expectations will in turn shape contracts, investor questions, supply chain expectations, and other drivers for responsible business conduct." Hum. Level, The EU Corporate Sustainability Due Diligence (EU CSDDD): The Final Text 3 (2024), https://cdn.prod.website-files.com/626132a21ac8ac2deb688aca/6608213467eb3e157a55d2c2_Human%20Level%20-%20EU%20CSDDD%20Overview%20-%2022%20March%202024%20-%20Final.pdf.

26. Eur. Comm'n, Study on due diligence requirements through the supply chain, 218 (2020) (finding that "[c]ontractual provisions and supply chain codes of conduct remain one of the most frequently used tools for implementing supply chain due diligence").

for performance with their business partners. Contracts are also legal instruments, meaning that the commitments and performance standards they contain are binding, even in the absence of local (or other) legislation. This is why contracts can fairly be described as the legal links of global supply chains. Understanding their significance, the CSDDD drafters have, in each iteration of the Directive's text, carved out a special role for contracts in carrying out HREDD.[27] Indeed, contracts feature prominently in Article 10 on preventive measures and Article 11 on corrective measures, and Article 18 on model contractual clauses states that the European Commission itself will develop guidance on contracts to help companies comply with the Directive. [28]

There is little doubt that the CSDDD will further increase the relevance and use of contracts as tools for implementing HREDD in supply chains, so it is important to get them right. This article analyzes the text of the legislation to offer practical answers to the question of "what do due diligence-aligned contracts look like." It proceeds by explaining how companies typically integrate HRE issues into their contracts, highlighting how traditional, risk-shifting, models of contracting are likely to fall short of the CSDDD requirements. It then explains the shared-responsibility approach to contracting, which contractualizes and operationalizes the collaboration principles embedded in the UNGPs and the OECD Guidelines and Guidance. It argues that, as compared with the traditional model, the shared-responsibility approach is better aligned with the CSDDD and is therefore a safer compliance bet for in-scope companies. [29] It closes with an actionable list of dos and don'ts

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27. *See* EUR. COMM'N, *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 (Feb. 23, 2022); Dadush, *Prosocial Contracts*, *supra* note 18, at 169.

28. CSDDD, *supra* note 1, art. 18 ("In order to provide support to companies to facilitate their compliance with Article 10(2), point (b), and Article 11(3), point (c), the Commission, in consultation with Member States and stakeholders, shall adopt guidance about voluntary model contractual clauses, by 26 January 2027.").

29. Recitals 46 and 54 both say that "contractual assurances should be designed to ensure that responsibilities are shared appropriately by the company and the business partners." *Id.* recitals 46, 54. Recital 66, referring to the Commission's guidance on model contractual clauses under Article 18, says that "the guidance should aim to facilitate a clear allocation of tasks between contracting parties and ongoing cooperation, in a way that avoids the transfer

for due diligence-aligned contracting, drawing attention to the work of the European Working Group for Responsible and Sustainable Supply Chains to draft model clauses (the European Model Clauses or EMCs) that are designed to track the CSDDD.[30]

A last note before launching into the analysis: We want to underscore that, while contracts are important vehicles for implementing effective HREDD, they are not a silver bullet: Companies cannot expect their HRE issues to be solved simply by changing their contracts. HREDD is a comprehensive process that extends far beyond contracts and requires continuous engagement with stakeholders, including suppliers and rights-holders, and monitoring. Likewise, while contracts are an important component of a robust HREDD process, they are not a proxy for it: Companies cannot expect to meet the CSDDD requirements simply by adding certain clauses to their contracts. This is addressed in the CSDDD Recitals, which clarify that companies cannot 'contract their way out' of their due diligence obligations.[31] Contracts can and should be (re) designed to strengthen the foundation for effective HREDD, but even the best contracts cannot replace HREDD—they can only facilitate it.

I.
The Problem with Traditional Contracts

Contracts make it possible for companies to implement their own HRE policies and standards across borders and their supply chains in a legally binding fashion. This is why companies rely heavily on their contracts, they give companies a legal tool to police their supply chains, even in the absence of national legislation—or, as is often the case, in the absence of enforced national legislation. Further, unlike national legislation, contracts are legal instruments that companies can

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of the obligations provided for in this Directive to a business partner and automatically rendering the contract void in case of a breach." *Id.* recital 66.

30. *The European Model Clauses*, European Working Group For Responsible and sustainable supply chains, https://www.responsiblecontracting.org/emcs (last visited Feb. 10, 2025).

31. CSDDD, note 1, recital 66 clarifies that the Commission's guidance on model contract clauses "should reflect the principle that the mere use of contractual assurances cannot, on its own, satisfy the due diligence standards provided for in this Directive."

shape and control directly.[32] Unfortunately, while contracts are widely used to manage supply chain risks,[33] they are often *mis*-used when it comes to managing HRE risks. When buyer companies include HRE obligations in their agreements with suppliers, they often place the risks, obligations, and costs associated with upholding HRE standards on the supplier.[34] This is

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32. *Decent Work Toolkit for Sustainable Procurement: Responsible Contracting in Sustainable Procurement*, UN Global Compact, [hereinafter, *Decent Work Toolkit*] https://sustainableprocurement.unglobalcompact.org/what-is-responsible-contracting/ (last visited June 17, 2025).

33. The inclusion of codes of conduct and human rights policies in commercial contracts is an increasingly common feature of supply chain management, as explained by various scholars and practitioners. *See, e.g.*, Eur. Comm'n, Study on due diligence requirements through the supply chain, *supra* note 26; Fabrizio Cafaggi, *Regulation Through Contracts: Supply-Chain Contracting and Sustainability Standards*, 12 Eur. Rev. Cont. L. 218, 218–58 (2016) (highlighting that because "quality" and "process" are increasingly driving global competition, sustainable-sourcing policies and codes are becoming influential tools to regulate and advance sustainability via commercial contracts); Kishanthi Parella, *Protecting Third Parties in Contracts*, 58 Am. Bus. L. J. 327, at 331, 337 (2020) [hereinafter Parella, *Protecting Third Parties in Contracts*] (explaining that multinational companies often include codes of conduct in supply contracts to address human rights risks); David Snyder, *The New Social Contracts in International Supply Chains*, 68 Am. U.L. Rev. 1869, at 1870, 1884–85 (2019) (detailing strategies for making human rights policies that are incorporated into supply contracts not just "legally effective" but also "operationally likely"); *see also* Jodi L. Short et al., *Monitoring Global Supply Chains* (Harv. Bus. Sch. Tech. & Operations Mgt. Unit Working Paper No. 14-032, U.C. Hastings Research Paper No. 84, 2015) (discussing how codes of conduct are frequently contractually imposed for labor and environmental standards, with thousands of multinational corporations monitoring supply-chain compliance via third-party private audits and finding that performance assessments are shaped by factors that often undermine their integrity).

34. *See* John F. Sherman III, *Integrating Human Rights Due Diligence into Model Supply Chain Contracts* 9 (Harvard Kennedy School, Working Paper No. 80, 2022) (explaining that buyers should not "offload" their due diligence responsibilities to suppliers); Jeffrey Vogt et al., *Farce Majeure: How Global Apparel Brands Are Using The COVID-19 Pandemic To Stiff Suppliers and Abandon Workers*, Worker Rts. Consortium 2 (2020) [hereinafter Vogt et al., *Farce Majeure*] (explaining that, in the apparel supply chain, "[t]he unequal relationship between brands and their suppliers manifests itself in purchase orders, which are largely contracts of adhesion, i.e. take-it-or-leave-it agreements — a point confirmed by many suppliers. Such contracts maximize the rights and interests of the party offering the contract, who will require that the other party accept the terms without negotiation, even though they are quite disadvantageous to the latter. In the case of the garment industry, brands and retailers draft these standard contracts, which are imposed upon the suppliers. The particulars of individual orders are negotiated within the standard contract framework. Notably, brands commonly use their leverage to require suppliers to assume and finance all risks. This includes forcing factories to borrow in

because traditional contracts focus on reducing legal exposure and managing companies' financial and reputational risks, not HRE risks. The company-risk focus encourages using the contract to push as much risk as possible from the buyer's side of the contractual balance sheet onto the supplier's side. To achieve this, traditional contracts rely on supplier-only guarantees (strict liability) of perfect compliance with HRE standards and punish imperfection with order cancellations, suspension of payments, and contract termination.[35]

To formalize risk-shifting, suppliers are often required to make a contractual promise (by way of a representation or a warranty[36]) that there are no HRE violations anywhere in the supply chain. Such promises are unrealistic: There is no such thing as a perfectly clean supply chain, so to require perfection

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order to operate while awaiting payment (which does not occur until after the clothes sell to the consumer)."); John F. Sherman III, *Irresponsible Exit: Exercising Force Majeure Provisions in Procurement Contracts*, 6 Bus. & Hum. Rts. J. 127, 128–29 (2020) [hereinafter Sherman, *Irresponsible Exit*].

35. Vogt et al., *Farce Majeure, supra* note 34 (including examples of clauses from major brands' (e.g., Kohl's, Topshop, Primark) supply contracts that illustrate the risk-shifting nature of commercial contracts and explaining how these lopsided clauses were recklessly and opportunistically activated during the COVID-19 pandemic); *see also* Sherman, *Irresponsible Exit, supra* note 36 (explaining how the often abusive use of force majeure clauses produced serious adverse impacts for workers and flew against the UNGPs, which many implicated companies subscribe to and commit to abide with); David V. Snyder, Susan Maslow & Sarah Dadush, *Balancing Buyer and Supplier Responsibilities: Model Contract Clauses to Protect Workers in International Supply Chains, Version 2.0*, 77 Bus. L. 115, 125-126 (2022) [hereinafter Snyder et al., *Balancing Buyer and Supplier Responsibilities*] (explaining the problem with relying on unrealistic, strict liability representations and warranties for ensuring the protection of workers and the move toward a standard of care model).

36. As an example of a warranty pertaining to HRE matters, here is a clause inspired by the first version of the Model Contract Clauses (MCCs 1.0) developed by a working group of the American Bar Association's Business Law Section in 2018: "Supplier represents and warrants to Buyer, on the date of this Agreement and throughout the contractual relationship, that Supplier and its subcontractors are in compliance with Buyer's Code of Conduct (Code) attached hereto. Each shipment and delivery of Goods shall constitute a representation by Supplier of compliance with the Code; such shipment or delivery shall be deemed to have the same effect as an express representation." David V. Snyder & Susan A. Maslow, *Human Rights Protections in International Supply Chains – Protecting Workers and Managing Company Risk*, A.B.A. Bus. L. Section 1093, 1097 (2018); *see also Decent Work Toolkit, supra* note 32. For more on the shortcomings of requiring perfect compliance from suppliers, see *The Core Principles of Modern Contracting*, Responsible Contracting Project [hereinafter *Core RCP Principles*] https://www.responsiblecontracting.org/principles.

contractually often places the supplier in breach on day one.[37] Besides being unrealistic, however, these promises are also dangerous because they incentivize suppliers to hide infractions out of fear of losing the contract and other contractual penalties. This pushes infractions further out of the buyer's view, where they are even less likely to be identified, let alone addressed or remediated. In other words, risk-shifting, expecting perfect compliance, and punishing imperfection can actually aggravate HRE risks by incentivizing deception, disincentivizing transparency, and making it much harder to address HRE problems, which are bound to arise.[38]

HREDD requires identifying and addressing HRE risks through ongoing, risk-based, proactive engagement.[39] It does not outlaw imperfection but rather accommodates it as a matter of course. Traditional contracts that formalize a legal fiction of perfect compliance set the supplier up for failure and incentivize non-transparency and non-compliance. This is why traditional contracts are not fit for purpose when it comes to managing HRE risks in global supply chains. When it comes to preventing adverse HRE impacts, therefore, risk-shifting is not the same thing as risk management.

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37. Snyder et al., *Balancing Buyer and Supplier Responsibilities*, *supra* note 35, at 126 ("The move from representation-and-warranty to due diligence is eminently practical, then, and should be reassuring to the parties. The participants in the supply chain are no longer being asked, unrealistically and fictitiously, to literally guarantee perfect compliance with the human rights and safety standards in Schedule P [supplier code of conduct] and the principled purchasing practices in Schedule Q. Instead, they are being required to be duly diligent, on an ongoing basis, about achieving those goals. This is not mere aspiration; the parties are contractually obligated to use reasonable means to achieve the goal. But there is no longer strict liability for failure of perfect compliance. And there is no longer the knowledge, certain to both parties, that the human rights obligations of the contract are breached the moment it is signed.").

38. Every sector is touched by human rights issues, whether it be forced labor, child labor, union busting, gender discrimination, illegal land grabs, wage theft, etc. *See generally List of Goods Produced by Child Labor or Forced Labor*, Bureau of Int'l Lab. Aff., https://www.dol.gov/agencies/ilab/reports/child-labor/list-of-goods (last visited June 17, 2025) (showing statistics on child labor); *ILO issues wage protection guidance for migrant workers*, Int'l Lab. Org. (Apr. 27, 2023), https://www.ilo.org/resource/news/ilo-issues-wage-protection-guidance-migrant-workers (discussing wage theft).

39. UNGP, *supra* note 15, at 22, 23; OECD Guidelines, *supra* note 16, at 27; Shift, *FAQs: on the EU Corporate Sustainability Due Diligence Directive (CS3D)*, 2-5 (2024); German Fed. Off. for Eco. Aff. and Exp. Controls, *Identifying, weighting and prioritizing risks*, 4, 11, 13 (2022).

For contracts to be appropriate and effective as preventive and corrective measures under the CSDDD, the traditional one-sided, strict compliance model of contracting should be set aside in favor of a due diligence-aligned model that is cooperation-based, dynamic, responsive and supported by responsible purchasing practices. This article's analysis of the CSDDD indicates that traditional contracting techniques will likely not "cut the mustard" under the new regime and that a different approach, rooted in the shared-responsibility principles enshrined in the UNGPs and the OECD Guidelines and Guidance is much more likely to pass the CSDDD test.

II.
Moving Toward a Shared-Responsibility Model of Contracting

As our analysis of the CSDDD text shows, in order to adhere to the requirements of the Directive, companies will need to move away from traditional, risk-shifting approaches to contracting toward a shared-responsibility approach. In brief, this means aligning the contract with the shared-responsibility principles enshrined in the UNGPs, the OECD Guidelines, and the OECD Guidance, which say that *all* businesses—regardless of their size, geographic location, sector, position in the supply chain, etc.—have a responsibility to respect human rights ("R2R") through HREDD.[40] This responsibility cannot simply be contracted away. As we explained in *Complying with Mandatory Human Rights Due Diligence Legislation through Shared-Responsibility Contracting: The Example of Germany's Supply Chain Act (LkSG)*, "a company's R2R cannot be shifted or delegated to others—contractually or otherwise. Each business has its own R2R to meet, in other words. In this way, the R2R, much like the human rights it is intended to respect, is inalienable—all businesses are

40. For a more detailed discussion of the UNGPs and the OECD Guidance with respect to shared responsibility, see Dadush et al, *Complying with Mandatory Human Rights Due Diligence*, *supra* note 15, at 259–64 (discussing the UNGPs and the OECD Guidance with respect to shared responsibility); Dadush, *Prosocial Contracts*, *supra* note 18 at 160, 166–69 (2022); Olivia Windham Stewart & Sarah Dadush, *Sharing Responsibility for Human Rights in Contracts*, BL (Sept. 2021), www.bloomberglaw.com/external/document/X8VLBTRO000000/commercial-professional-perspective-sharing-responsibility-for-h.

born with it and must meet it for as long as they are in business; it cannot be taken or given away."[41]

HREDD, the mechanism through which companies discharge their R2R, is suffused with shared responsibility. First, by its nature, HREDD requires cooperation across the supply chain. It is not, and cannot realistically be, a solo operation—it is a joint endeavor. Indeed, every step of HREDD requires cooperation, from identifying risks, to collecting and communicating information about those risks, to preparing and implementing preventive and corrective action plans, all the way to remediation.[42] Even the most dedicated-to-HRE business will be limited in what it can achieve on its own; for in-scope companies, the cooperation-stakes are higher as effective HREDD is now a matter of legal compliance, not just voluntary compliance. Second, attempts to offload HRE risks and responsibilities to business partners—especially partners who lack the necessary capacity and resources—would go against both the UNGPs and the OECD standards. The OECD Guidance makes the point clearly:

Due diligence does not shift responsibilities. *Each enterprise in a business relationship has its own responsibility to identify and address adverse impacts.* The due diligence recommendations of the OECD Guidelines for MNEs . . . recommend that each enterprise addresses its own responsibility with respect to adverse impacts.[43]

In fact, to the extent risk-shifting is contemplated under the UNGPs and the OECD standards, it is to *increase* lead firms' responsibilities, not decrease them. Indeed, under the standards, all businesses must avoid causing, contributing, or being directly linked to adverse impacts; should one company fail to discharge its HREDD responsibilities, the R2R for other companies in the supply chain would deepen as they would be responsible for picking up the slack.[44] In sum, although lead firms might like it to be otherwise, the responsibility for HREDD is non-delegable. This is so under the UNGPs, the OECD Guidelines and Guidance, and, as shown below, the CSDDD. To be effective, HREDD requires companies to cooperate and share responsibility for

41. Dadush et al, *Complying with Mandatory Human Rights Due Diligence*, *supra* note 15, at 260.

42. *Id.*

43. OECD Guidance at 17 (2018) (emphasis added).

44. Dadush, *Prosocial Contracts*, *supra* note 18, at 168–69.

upholding HRE standards, even and especially when things go wrong. Commercial contracts, as critical components of the HREDD ecosystem, should therefore be designed accordingly, to reflect and formalize shared responsibility.

There are now several tools that companies can employ to 'upgrade' their contracts to embed shared responsibility, including model clauses, template codes of conduct, and implementation guidance.[45] Additionally, the Responsible Contracting Project identifies three core principles (the "3Rs" of Responsible Contracting) that support integrating shared responsibility into commercial contracts in alignment with the UNGPs, the OECD Guidelines and Guidance, and mandatory HREDD legislation:[46]

1) Responsibility for human rights and the environment is shared: The parties should jointly commit to cooperate to carry out HREDD and to proactively address HRE problems as they arise. Risks and obligations should be fairly and reasonably allocated between the parties, considering their respective resources and capacities. (Risk-sharing, not risk-shifting).
2) Responsible purchasing practices: Buyers, including suppliers when they act as buyers, should commit to responsible sourcing and purchasing practices as part of their HREDD. They should further commit to regularly evaluate how their practices support (or undermine) HREDD and make necessary adjustments to ensure that their practices do not aggravate HRE risks and contribute to positive HRE performance.
3) Remediation first and Responsible exit: The parties should jointly commit to prioritize

45. The Responsible Contracting Project's Toolkit includes various model clauses, template codes of conduct, and implementation guidance developed in collaboration with different partners including, the American Bar Association Business Law Section Working Group to Draft Model Contract Clauses to Protect Human Rights in International Supply Chains, the European Working Group for Responsible and Sustainable Supply Chains, the Interfaith Center for Corporate Responsibility, the Sustainable Terms of Trade Initiative, and the UN Global Compact, among others. *RCP Toolkit*, Responsible Contracting Project, https://www.responsiblecontracting.org/toolkit (last visited June 17, 2025).

46. *Core RCP Principles*, *supra* note 36.

> rightsholder-centered remediation in the event of an adverse impact, ahead of, or in conjunction with, conventional contract remedies, such as order cancelation, suspension of payments, rejection of goods, and termination. If the buyer contributed to the impact, then it must provide remediation at least in proportion to its contribution. The parties should further commit to pursue exit or termination only as a last resort and to take appropriate measures to mitigate the impacts of exit.

The key language of the CSDDD that supports our argument that due diligence-aligned contracting is, in essence, shared-responsibility contracting, can be found in Recitals 46, 54, and 66. Specifically, Recitals 46 and 54 both clarify that "[c]ontractual assurances should be designed to ensure that *responsibilities are shared appropriately* by the company and the business partners."[47] Further, Recital 66, which accompanies Article 18 on the Commission's guidance on model contractual clauses[48] says that: "The guidance should aim to facilitate a clear allocation of tasks between contracting parties and *ongoing cooperation*, in a way that *avoids the transfer of the obligations provided for in this Directive to a business partner and automatically rendering the contract void in case of a breach.* The guidance should reflect the principle that the mere use of contractual assurances cannot, on its own, satisfy the due diligence standards provided for in this Directive."[49]

III.
Shared Responsibility in the CSDDD

As highlighted above, it is critical to understand that the due diligence obligations laid out in the CSDDD are mainly obligations of means, not results.[50] This means that, in order to comply with the CSDDD, companies must meet a certain standard of care in developing and implementing preventive and corrective measures. Importantly, companies are not expected

47. CSDDD, *supra* note 1, recitals 46, 54 (emphasis added). Contractual assurances are required appropriate measures (where relevant) under Articles 10 and 11. *Id.* arts. 10, 11.

48. *Id.* art. 18.

49. *Id.* recital 66 (emphases added).

50. *Id.* recital 19.

to have zero (potential and actual) adverse impacts in their chain of activities. Rather, they are expected to have a robust risk-management system in place to proactively identify, prioritize, and address impacts. As such, the CSDDD does not create a strict liability regime for in-scope companies, but rather a continuous improvement regime. To make this system work, cooperation along the supply chain is essential. As explained in the previous Part, it is not possible for companies to carry out effective HREDD alone; they must communicate and work together to find and solve problems. Just as shared responsibility is part of the fabric of the UNGPs, so too is it part of the fabric of the CSDDD.

While the CSDDD imposes an obligation for companies to conduct HREDD, it does not specify a rigid formula for doing so. There is, in other words, no one size fits all when it comes to due diligence. Each company will be expected to demonstrate that it is "doing its homework" to identify, prevent, mitigate, and, as needed, remediate adverse impacts in its chain of activities. This process-based regime gives companies a lot of flexibility in how they design and implement due diligence measures, including their contracts. This flexibility is not boundless, however: Companies must employ *appropriate measures* to carry out their due diligence, as defined in Article 3(1)(o) and further set out in Articles 10(1) and 11(1).[51] To be appropriate, due diligence measures must be *effective*, meaning that they must be designed and evaluated on the basis of their capacity to actually achieve the objectives of HREDD.[52] In addition, Article 15 (Monitoring) states that due diligence measures, including contracts, must be regularly monitored for effectiveness to ensure that they are in fact doing the job they were designed to do.[53]

The requirement of appropriateness sets boundaries around how companies can meet their due diligence obligations, limiting companies' ability to simply tick-box their way to compliance.[54]

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51. *Id.* arts. 3(1)(o), 10(1), 11(1).

52. *Id.* art. 3(1)(o).

53. *Id.* art. 15 (requiring Member States to ensure that companies carry out periodic assessments of their own operations and measures, as well as those of their subsidiaries and business partners, to assess and monitor the adequacy and effectiveness of the due diligence process).

54. Nadia Bernaz et. al., *The EU Directive on Corporate Sustainability Due Diligence (CSDDD): The Final Political Compromise*, 9 Bus. & Hum. Rts. J. 3–4 (2024).

A. *Contracts Must Be Appropriate*

The CSDDD identifies contracts as preventive and corrective measures that companies will be expected to employ, where relevant and feasible, to meet their due diligence obligations. Article 10 (Preventing Adverse Impacts) and Article 11 (Bringing Actual Adverse Impacts to an End), both speak directly to contracts and require companies to "seek contractual assurances from direct business partners that they comply with the company's code of conduct and, as necessary, with the company's prevention action plan" or with the company's "corrective action plan."[55] As preventive measures, contracts must be designed "to prevent or, where prevention is not possible or not immediately possible, adequately mitigate, potential adverse impacts that have been or should have been identified."[56] As corrective measures, contracts must be designed, in combination with other measures, "to bring actual adverse impacts that have been, or should have been, identified . . . to an end."[57]

Articles 10(1) and 11(1) instruct that, unless contracts are appropriate, they will fall short of meeting the new legal requirements. This begs the question: What is an appropriate, due diligence-aligned contract? What contracting practices does the CSDDD rule out and in?

For contracts to be appropriate, they need to be capable of *effectively* addressing adverse impacts in a way that is commensurate with the severity and likelihood of the impact, as well as with the company's level of involvement in the impact.[58] Account must be taken of "the circumstances of the specific case, including the

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55. CSDDD, *supra* note 1, arts. 10(2)(b), 11(3)(c) state that companies must "seek contractual assurances from a direct business partner that it will ensure compliance with the company's code of conduct and, as necessary, a prevention action plan [or corrective action plan], including by establishing corresponding contractual assurances from its partners, to the extent that their activities are part of the company's chain of activities."

56. *Id.* art. 10(1).

57. *Id.* art. 11(1).

58. *Id.* art. 3(l)(o) generally defines the principle of appropriateness. Articles 10(1) and 11(1) set forth additional appropriateness criteria in relation to preventive and corrective measures. When designing appropriate measures, companies should consider the degree and nature of a company's involvement in an adverse impact (cause, jointly cause, directly linked); whether the adverse impact could (or did) occur in the company's own operations or in those of a subsidiary, a direct business partner, or an indirect business partner; and how much influence the company has over the business partner that could (or did) cause or jointly cause the adverse impact. *Id.* arts. 10(1), 11(1).

nature and extent of the adverse impact and relevant risk factors."[59] Therefore, rather than operating on their own, contracts must be designed to support a broader, context-specific, and dynamic process for identifying, preventing, mitigating potential adverse impacts and for correcting and remediating actual adverse impacts. The Recitals provide further guidance regarding what types of contracts the legislators would deem appropriate and due diligence-aligned: Contracts must be designed to share responsibilities appropriately between the parties and include a clear allocation of tasks to facilitate cooperation; they must also avoid simply transferring HREDD obligations.[60]

Here are some factors to consider in determining the appropriateness of due diligence measures, including contracts:

Company involvement: The closer the company is to a (potential or actual) adverse impact, the more involved it is in that impact, the greater the due diligence expectation will be. Specifically, companies should design contracts in a way that accounts for the possibility that adverse impacts could be caused jointly by the company and a subsidiary or business partner, or caused solely by a business partner.[61]

Severity and likelihood: The more severe and likely the impact, the greater the due diligence expectation will be.

Influence: The more influence the company has on business partners that are causing or jointly causing adverse impacts, the greater the due diligence expectation will be. Influence also matters for determining what type(s) of measures to employ in order to effectively address adverse impacts. That said, the

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59. *Id.* art. 3(1)(o). "'[R]isk factors' means facts, situations or circumstances that relate to the severity and likelihood of an adverse impact, including company-level, business operations, geographic and contextual, product and service, and sectoral facts, situations or circumstances." *Id.* art. 3(1)(u).

60. Even though recitals are not binding, they are regularly used to interpret the text of EU legislation, particularly to resolve issues of clarity. Recitals 46, 54, and 66 provide useful guidance to interpret what "appropriateness" means for contractual obligations and purchasing practices. CSDDD, *supra* note 1, recitals 46, 54, 66.

61. *Id.* arts. 10(1)(a), 11(1)(a). When designing appropriate measures, companies should consider the degree and nature of a company's involvement in an adverse impact (cause, jointly cause, directly linked); whether the adverse impact could (or did) occur in the company's own operations or in those of a subsidiary, a direct business partner, or an indirect business partner; and how much influence the company has over the business partner that could (or did) cause or jointly cause the adverse impact. *Id.* arts. 10(1), 11(1).

CSDDD recognizes that companies are not always able to influence the conduct of the businesses in their chain of activities. Thus, the appropriateness criteria include the company's "ability to influence the business partner that may cause or jointly cause the potential adverse impact".[62] This leaves some allowance for companies with little influence. Nevertheless, even companies that have little (or no) influence are expected to take measures to increase their influence, which could include contracting with indirect business partners.[63]

Appropriateness gives companies latitude in designing their due diligence measures, shielding them from unrealistic, prescribed, one-size-fits-all requirements. But it also restricts that latitude by establishing due diligence criteria: Not just any due diligence measures will do, only appropriate and effective ones. If the Directive protects in-scope companies from unrealistic due diligence requirements, requiring in-scope companies to employ (only) measures that are "reasonably available" to them and that reflect their contributions and ability to influence, then it stands to reason that businesses that are not in-scope for the Directive, but are involved in an in-scope company's chain of activities should have at least the same protection. Otherwise put, in-scope companies should not use their contracts to impose more stringent, unrealistic, or unnecessarily burdensome HREDD requirements on their business partners than they are themselves subject to.

In this way, the appropriateness criteria inform not only the expectations of in-scope companies, but also the due diligence expectations of in-scope companies vis-a-vis their business partners. Contractual obligations should be formulated according to the same appropriateness standard, considering the partner's capacity, influence, and what HREDD measures are "reasonably available" to them.

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62. *Id.* arts. 10(1)(c), 11(1)(c).

63. *Id.* art. 10(4) ("As regards potential adverse impacts that could not be prevented or adequately mitigated by the appropriate measures . . . the company may seek contractual assurances from an indirect business partner, with a view to achieving compliance with the company's code of conduct or a prevention action plan."). *Id.* art. 11(5) ("As regards actual adverse impacts that could not be brought to an end or the extent of which could not be adequately minimised by the appropriate measures . . . the company may seek contractual assurances from an indirect business partner, with a view to achieving compliance with the company's code of conduct or a corrective action plan.").

B. *The Do's and Don'ts of Due Diligence-aligned Contracting*

The Directive, including the Recitals, sets out key principles for understanding what appropriate contracts looks like. The below provides an overview of the types of contracting practices that companies should avoid, and which they should pursue, to be in sync with the new EU regime.

1. *Promote Cooperation*

Companies should use contracts to establish a solid foundation for the parties to cooperate in carrying out HREDD, not to transfer due diligence responsibilities to business partners or to require perfect HRE compliance.

Due diligence requires each actor in the chain to do their part to address adverse impacts and be accountable for their involvement in such impacts. Recitals 46 and 54 clarify that contracts must be designed to ensure that HREDD obligations are *shared* appropriately between the parties, not simply imposed on business partners.[64] This is reinforced by Recital 66, which underlines that contracts should not be used to transfer the legal obligations of the Directive to business partners and that the contract should clearly allocate tasks to both parties.[65]

Thus, contracts that place obligations only on the supplier are fundamentally out of sync with the CSDDD. The Directive further states that, as preventive and corrective measures, contracts must reflect the degree to which a company could jointly cause an impact.[66] A contract that obliges only the business partner to uphold HRE standards does not adhere to this requirement because it allows buyers to contractually wash

64. *Id.* recitals 46, 54. Recitals 46 and 54 both contain similar language in this regard: "*Contractual assurances should be designed to ensure that responsibilities are shared appropriately by the company and the business partners.* The contractual assurances should be accompanied by appropriate measures to verify compliance. However, the company should only be obliged to seek the contractual assurances, as obtaining them may depend on the circumstances." *Id.* (emphasis added).

65. *Id.* recital 66. Recital 66, which deals with the guidance on model contract clauses to be developed by the European Commission, clarifies that "[t]he guidance should aim to facilitate a clear allocation of tasks between contracting parties and ongoing cooperation, in a way that avoids the transfer of the obligations provided for in this Directive to a business partner and automatically rendering the contract void in case of a breach." *Id.*

66. *Id.* arts. 10(1), 11(1).

their hands of an adverse impact, even if they jointly caused (contributed) it.[67]

Furthermore, while one-sided contractual guarantees of perfection (e.g., representations and warranties that are usually imposed on the weaker, production-country supplier) are simple to draft and enforce, they are not appropriate for HREDD purposes because, as explained above, they are unrealistic and dangerous. Strict compliance clauses that say something to the effect of, "the supplier shall comply with the code of conduct and any violation shall constitute a material breach of contract" can aggravate HRE risks. As mentioned, if the contract says that the buyer can, at the first sign of trouble, contractually sanction suppliers, immediately cancel an order, suspend payments, or terminate the relationship altogether, this could make the business partner reluctant to disclose problems. In fact, it may incentivize the partner to hide problems, which will make it harder for the in-scope company not only to identify adverse impacts (e.g., via due diligence questionnaires, audits, or supplier interviews), but also to design and implement measures to effectively address the impacts, as required by the CSDDD.

A critical shortcoming of strict liability clauses is that they do not speak to the prevention, correction, or remediation aspects of HREDD, all of which are central to CSDDD compliance. This, combined with the incentives they create for partners to hide HRE problems, makes strict liability clauses ill-suited for HREDD. They are also not commensurate with the likelihood of impacts, which, in many (if not all) supply chains, cannot be completely eradicated. Since adverse impacts are likely, obliging suppliers to meet a zero-adverse-impact standard is not appropriate.[68] Another reason why strict compliance clauses are not appropriate is because they ask suppliers and business partners to make perfection-promises they cannot keep, which often place suppliers in breach of contract on day one. This again fails to meet the CSDDD's appropriateness criteria, which instructs that due diligence measures must be

67. The CSDDD addresses the responsibility of buying companies to avoid contributing to adverse impacts at the supplier level in Articles 10(1)(a) and 11(1)(a) and in Recitals 45 and 53. *Id.* The issue also comes up specifically in relation to purchasing, distribution, and design practices, which are addressed in Articles 10(2)(d), 11(3)(e) and in Recitals 46, 47, 54, *id.*, discussed in more detail below.

68. *See* CSDDD, *supra* note 1, art. 10(1)(c), 11(1)(c).

"reasonably available" to the parties.[69] The impossible is not a reasonably available solution.

Because companies will be required to conduct due diligence in their own operations, their subsidiaries' operations, and those of the businesses involved in their chain of activities,[70] cooperation and transparency with business partners are essential. To enhance cooperation and transparency contractually, the agreements should set out a joint commitment by both parties to cooperate in carrying out risk-based HREDD, in an ongoing fashion and throughout the life of the contract, as well as a clear allocation of tasks reflecting the shared responsibility of both parties to uphold HRE standards.[71] This means setting realistic obligations for both parties, taking into account their respective capacities and circumstances. If one of the parties is a small or medium-sized enterprise ("SME"), it may be more appropriate for them to commit to cooperating in the buyer's HREDD process, rather than setting up their own.

Yet another shortcoming of risk-shifting contracts is that they create a legal fiction that only the partner is responsible for HREDD, ignoring that the CSDDD requires due diligence measures to take into account the company's own level of involvement in (potential and actual) adverse impacts—causing or jointly causing.[72] This means that in-scope companies must address how their own practices do or could contribute to adverse impacts, which in turn brings purchasing practices into view. More on this just below.

2. *Consider Purchasing Practices and Their Impacts*

Companies must consider how purchasing practices can contribute to adverse impacts and include a contractual commitment to responsible purchasing practices from day one.

The CSDDD clarifies that companies are responsible not only for adverse impacts they cause directly, but also for impacts

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69. CSDDD, *supra* note 1, art. 3(1)(o) ("'appropriate measures' means measures that are . . . reasonably available to the company, taking into account the circumstances of the specific case, including the nature and extent of the adverse impact and relevant risk factors.").

70. The CSDDD defines the chain of activities to include the upstream supply chain and a share of the downstream value chain limited to distribution, transport, and storage of goods. *Id.* art. 3(1)(g).

71. *See id.* recitals 46, 54, 66.

72. *Id.* art. 10(1).

they jointly cause ("contribute to" in UNGP terminology) through their own actions and omissions.[73] Joint causation covers behaviors that incentivize adverse impacts,[74] such as poor purchasing practices, and, by extension, commercial contracts that formalize or otherwise allow such practices. Companies will need to assess whether and how their purchasing practices are likely to create risks and to adapt[75] them accordingly: "Where relevant, companies should adapt business plans, overall strategies and operations, including purchasing practices, and develop and use purchasing policies that contribute to living wages and incomes for their suppliers, and that do not encourage potential adverse impacts on human rights or the environment." [76]

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73. *Id.* art. 10(1), 11(1), recital 53.

74. *Id.* recital 53 ("Jointly causing the adverse impact is not limited to equal implication of the company and its subsidiary or business partner in the adverse impact, but should cover all cases of the company's acts or omissions, causing the adverse impact in combination with the acts or omissions of subsidiaries or business partners, including where the company substantially facilitates or incentivises a business partner to cause an adverse impact, that is, excluding minor or trivial contributions.").

75. Articles 10(2)(d) and 11(3)(e) have similar language on this. "Companies shall be required to take the following appropriate measures, where relevant: . . . make necessary modifications of, or improvements to, the company's own business plan, overall strategies and operations, including purchasing practices, design and distribution practices." *Id.* arts. 10(2)(d), 11(3)(e). For a more in-depth analysis of this requirement, see Daniel Schönfelder & Michaela Streibelt, The obligations on responsible purchasing and responsible procurement established by the CSDDD *in* CSDDD Commentary (Bright & Scheltema eds.) (forthcoming 2025); [hereinafter Responsible Purchasing and the CSDDD].

76. CSDDD, *supra* note 1, recital 46, which reads, in whole: "Where relevant, companies should adapt business plans, overall strategies and operations, including purchasing practices, and develop and use purchasing policies that contribute to living wages and incomes for their suppliers, and that do not encourage potential adverse impacts on human rights or the environment. To conduct their due diligence in an effective and efficient manner, companies should also make necessary modifications of, or improvements to, their design and distribution practices, to address adverse impacts arising both in the upstream part and the downstream part of their chains of activities, before and after the product has been made. Adopting and adapting such practices, as necessary, could be particularly relevant for the company, to avoid an adverse impact in the first instance. Such measures could also be relevant to address adverse impacts that are jointly caused by the company and its business partners, for instance due to the deadlines or specifications imposed on them by the company. In addition, by better sharing the value along the chain of activities, responsible purchasing or distribution practices contribute to fighting against child labour, which often arises in countries or territories with high poverty levels."

The adverse impacts associated with purchasing practices vary between sectors and the power dynamics at play within different sectors, although they are known to be especially relevant in low-wage sectors with stark power imbalances between buyers and suppliers,[77] such as agriculture, textiles, transport,

77. On purchasing practices and how poor practices negatively impact human rights, see Mark Anner, *Squeezing Workers' Rights in Global Supply Chains: Purchasing Practices in The Bangladesh Garment Export Sector in Comparative Perspective*, 27 Rev. Int'l Pol. Econ. 320, 327–30 (2020); Parella, *Protecting Third Parties in Contracts*, *supra* note 33, at 340–41 and accompanying footnotes; Vogt et al., *Farce Majeure*, *supra* note 34; Better Buying Inst., Purchasing Practices and Factory-Level Noncompliances: How the Available Research Can Inform Supply Chain Due Diligence (2023), https://betterbuying.org/download/purchasing-practices-and-factory-level-noncompliances-how-the-available-research-can-inform-supply-chain-due-diligence/?wpdmdl=1969&refresh=67a7d0df9d52e1739051231; MSI Working Grp. on Responsible Purchasing Practices, The Common Framework for Responsible Purchasing Practices, Building Resilience in Textile Supply Chains 5–6 (2022), https://static1.squarespace.com/static/636ba8ae2fd47349a887dd92/t/642ecf75bca27075443eac29/1680789366782/CFRPP+full+Framework.pdf; *The Impact of Purchasing Practices on Workers' Human Right*s, Better Buying Inst., https://betterbuying.org/the-impact-of-purchasing-practices-on-workers-human-rights/ (last visited Jan. 10, 2025); Natasja Sheriff-Wells & Chana Rosenthal, A Broken Partnership: How Clothing Brands Exploit Suppliers and Harm Workers – And What Can Be Done About It, NYU Stern Ctr. for Bus. and Hum. Rts. (2023), https://bhr.stern.nyu.edu/wp-content/uploads/2024/01/NYUCBHRBrokenPartnership_ONLINEAPRIL3.pdf; *Reducing Supply Chain Risk by Buying Responsibly*, Ethical Trading Initiative, https://www.ethicaltrade.org/buying-responsibly (last visited Jan. 10, 2025); Oxfam H.K., Turning the Garment Industry Inside Out: Purchasing Practices and Workers' Lives (2004), https://www.oxfam.org.hk/tc/f/news_and_publication/1458/content_3562en.pdf; Sarah Labowitz & Dorothée Baumann-Pauly, Business as Usual is Not an Option: Supply Chains and Sourcing after Rana Plaza, NYU Stern Ctr. for Bus. and Hum. Rts. (2014), https://www.wiwiss.fu-berlin.de/forschung/Garments/Medien/2014_NYU_Bangladesh-Supply-Chains.pdf; Astha Rajvanshi, *Shein is the World's Most Popular Fashion Brand—at a Huge Cost to Us All*, TIME (Jan. 17, 2023), https://time.com/6247732/shein-climate-changelabor-fashion/; Daniel Vaughan-Whitehead & Luis Pinedo Caro, *Purchasing Practices and Working Conditions in Global Supply Chains: Global Survey Results*, Int'l Lab. Org. [ILO] INWORK Issue Brief No. 10 (June 2017), https://www.ilo.org/sites/default/files/wcmsp5/groups/public/%40ed_protect/%40protrav/%40travail/documents/publication/wcms_556336.pdf; Mengxin Li, Paying for a Bus Ticket and Expecting to Fly: How Apparel Brand Purchasing Practices Drive Labor Abuses, Hum. Rts. Watch (2019), https://www.hrw.org/sites/default/files/report_pdf/wrd0419_web2.pdf; Muhammad Azizul Islam et al., Impact of Global Clothing Retailers' Unfair Practices on Bangladesh Suppliers During Covid-19 (2023), https://www.abdn.ac.uk/media/site/business/documents/Impact_of_Global_Clothing_Retailers_Unfair_Practices_on_Bangladeshi_Suppliers_During_COVID-19.pdf; Mark

cleaning, and construction.[78] Examples of purchasing practices that can contribute to adverse impacts include, imposing prices that are too low to cover production costs, inflexibility on price adjustments even when input prices increase or market circumstances change, too-short lead times, too-long payment terms, frequent or last minute order changes, requiring adherence to rigorous HRE standards without providing assistance to support such adherence.[79]

Contracts should formalize purchasing practices that support—not undermine—positive HRE performance in a context and industry-specific manner. This means avoiding formalizing purchasing practices that are likely to create severe commercial pressures on suppliers, as such pressures can lead to adverse impacts. Companies should therefore adapt their contracts, including commercial terms, to avoid incentivizing poor HRE outcomes, starting with high HRE-risk product categories.

Furthermore, the CSDDD says that purchasing practices should be designed to "contribute to living wages and incomes for their suppliers."[80] This may, especially in low-wage sectors, require formulating pricing provisions that include a commitment to paying a living wage or income to the supplier's workers, as well as a process for calculating, ringfencing, and paying that price.[81] The effectiveness of these types of provisions would be enhanced by including a price escalation clause (or at least a commitment to renegotiate price terms) to allow

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Anner, Leveraging Desperation: Apparel Brands' Purchasing Practices during Covid-19, Ctr. for Glob. Workers' Rts. (2020), https://ler.la.psu.edu/wp-content/uploads/sites/26/2022/04/Leveraging-Desperation_October-16-2020.pdf; Better Buying Inst., Special Report: Cost and Cost Negotiation and the Need for New Practices (2020), https://betterbuying.org/wp-content/uploads/2020/07/Better-Buying-Special-Report-Cost-Cost-Negotiation-the-Need-of-New-Practices.pdf; Responsible Purchasing and the CSDDD, *supra* note 75.

78. Recital 47 specifically identifies only agriculture as a low-wage sector, CSDDD, *supra* note 1, recital 47, but the others in this list are known to be both low-wage and high risk.

79. *Id.*

80. *Id.* recital 46 ("Where relevant, companies should . . . use purchasing policies that contribute to living wages and incomes for their suppliers, and that do not encourage potential adverse impacts on human rights or the environment.").

81. For guidance, see ACT on Living Wages, *ACT Labour Costing Protocol*, https://actonlivingwages.com/app/uploads/2021/04/ACT-Labour-Costing-Protocol.pdf.

the contract price to increase in the event of an increase in production costs, such as the local minimum wage or input costs.

Given that poor purchasing practices are expressly identified in the Directive as a way that in-scope firms can "jointly cause" adverse impacts,[82] contracts that fail to address purchasing practices as a component of HREDD would not meet the Directive's appropriateness requirements. Contracts should therefore (a) identify responsible purchasing practices as a due diligence obligation and (b) include commitments to specific purchasing practices that are relevant for preventing adverse impacts in the supply chain at issue (e.g., pricing that includes HRE costs, transparent forecasting, order modifications, fair payment terms, providing financial and technical assistance to implement HREDD, accepting due diligence questionnaires prepared for other business partners when possible).

One-sided contracts that ignore the buyer's responsibility to prevent (or correct) adverse impacts—even those they contribute to via their purchasing practices—will likely be viewed as inappropriate for a few reasons. First, they fail to take the company's level of involvement in adverse impacts into account, as required by the CSDDD.[83] Here again one-sided contracts create a legal fiction where only the supplier is responsible for adverse impacts, which renders invisible the buyer's own contributions to the problem(s). This fiction allows companies to contract their way out of responsibility for adverse impacts. Second, such contracts fail to ensure that "responsibilities are

82. CSDDD, *supra* note 1, recital 46 ("Where relevant, companies should adapt business plans, overall strategies and operations, including purchasing practices, and develop and use purchasing policies that contribute to living wages and incomes for their suppliers, and that do not encourage potential adverse impacts on human rights or the environment. To conduct their due diligence in an effective and efficient manner, companies should also make necessary modifications of, or improvements to, their design and distribution practices, to address adverse impacts arising both in the upstream part and the downstream part of their chains of activities, before and after the product has been made. Adopting and adapting such practices, as necessary, could be particularly relevant for the company, to avoid an adverse impact in the first instance. Such measures could also be relevant to address adverse impacts that are jointly caused by the company and its business partners, for instance due to the deadlines or specifications imposed on them by the company. In addition, by better sharing the value along the chain of activities, responsible purchasing or distribution practices contribute to fighting against child labour, which often arises in countries or territories with high poverty levels.").

83. *Id.* arts. 10(1)(a), 11(1)(a).

shared appropriately"[84] as required by the CSDDD. Third, one-sided contracts undermine the effectiveness of the company's other due diligence measures: Including responsible purchasing commitments in the contracts gives suppliers the security, stability, and the assurance *they* need to effectively participate in the in-scope company's due diligence process to prevent and address adverse impacts. Fourth, without a contractual commitment to engage in responsible purchasing, it would be considerably more difficult (though not impossible[85]) to hold the buyer contractually accountable when their own conduct contributes to an adverse impact. Without such accountability, the buyer can place all the contractual blame for an adverse impact on the supplier and activate their self-help remedies (e.g., cancel orders, suspend payments, impose penalties, reject deliveries even of conforming goods, terminate the contract, etc.).

Compounding the problem, in the traditional, risk-shifting contractual set up, suppliers are deterred from alerting buyers to HRE problems, in particular problems connected to the buyer's practices, because they do not want to risk being seen as difficult to work with.[86] This is another reason why incorporating buyer responsibilities in the contract is important: It incentivizes the type of open communication, transparency, and trust that are critical for effective HREDD. It also offers context for understanding the CSDDD requirement that contracts include a clear distribution of HREDD-related tasks and responsibilities for both parties, not just the business partners.

Lastly, as part of good purchasing practices, companies can incentivize better HRE performance by committing to rewarding superior HRE performance by suppliers, for example,

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84. *Id.* recitals 46, 54.

85. *See* Sarah Dadush, Shared Responsibility in American Contract Law (unpublished manuscript) (on file with editors) (showing that American contract law makes much more room for shared-responsibility 'claims' than U.S. trained lawyers might expect, for example, through the implied covenant of good faith, implied terms (e.g., non-interference, cooperation, among others), and doctrines that address the pre and post-breach conduct by *both* parties, not just the breaching party. Similar, often clearer and more onerous, rules and doctrines operate in European (and other) jurisdictions to hold both parties accountable—in a sense as 'co-breachers'—for failing to do their respective parts to ensure contractual success. Such rules are more common in jurisdictions with civil or hybrid civil-common law systems where the 'borders' between contract and tort law are more fluid).

86. CSDDD, *supra* note 1, recitals 46, 54.

through contract renewals, longer-term contracts, additional investments (including to help improve access to finance), or higher order volumes. Such positive incentives are especially relevant in high-risk and low-wage sectors.

3. *Distribute Costs Fairly*

Companies should aim to include assistance and cost-sharing commitments in the contract to ensure that HREDD-related costs are distributed fairly and not simply passed on to business partners.

If a business partner lacks the capacity to meet an in-scope company's HREDD-related requirements or expectations, then pursuing that business relationship without providing support or assistance would likely violate the appropriateness requirement.[87] By extension, if the partner cannot reasonably be expected to perform HREDD-related obligations, then a contract containing such obligations cannot be considered appropriate.

To avoid transferring obligations or jointly causing impacts, in-scope companies must do their part to enable their business partners to meet HREDD-related requirements. This can be achieved by, for example, including price escalation or cost-sharing provisions in the contract to cover HREDD-related costs. To align with the Directive, companies should (at least) make a general contractual commitment to provide reasonable financial and technical assistance, where commercially feasible, to support the partner's performance of its HREDD-related obligations. Such commitments could be designed with greater specificity depending on how strategic a partner is (e.g., the share of the company's supply that is provided by the partner). If a company "prices in" HREDD-related costs this way, for example, by including a price escalation clause to adapt to rising minimum wages, then the business partner would not have to carry the costs alone, which would increase the likelihood of effective HREDD.

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87. *Id.* art. 3(o). Requiring a partner to implement measures that exceed its capacity is inappropriate because it is unrealistic and unreasonable, and therefore ineffective. Moreover, recalling that in-scope companies are only obliged to employ measures that are "reasonably available" to them, it is likely that requiring more of their business partners than what the CSDDD expects of in-scope companies will be seen as disproportionate, placing this type of measure even more firmly in the inappropriate 'box.'

Contractual HREDD requirements that create excessive burdens on suppliers, especially smaller ones (e.g., requiring small companies to establish their own full-fledged HREDD systems, carry out comprehensive risk assessments, set up expansive grievance mechanisms, complete endless one-size-fits-all due diligence questionnaires, obtain multiple certifications at their own cost, or receive unlimited audits) are likely to be viewed as constituting an inappropriate transfer of obligations. Moreover, the effectiveness of such requirements is questionable, since overwhelmed suppliers are less likely to implement required measures in a satisfactory manner. Lastly, these types of requirements can impose a stricter standard on business partners than on in-scope companies under the CSDDD. Recall that the CSDDD requires in-scope companies to employ only measures that are reasonably available to them; asking partners to do more than in-scope companies are asked to do could present a proportionality problem.

To be appropriate, contracts should set out joint, reasonable, and balanced HREDD obligations that include providing support to suppliers, especially those with limited resources and capacity. This would help to avoid overwhelming suppliers, particularly SME suppliers, with HREDD obligations, which is critical for effectiveness. In-scope companies should also commit to sharing costs associated with implementing and verifying the implementation of due diligence measures.[88] In the event of a potential or actual adverse impact that requires the preparation and implementation of a preventive or corrective action plan, the parties should share costs in proportion to each party's contribution to the adverse impact.[89] Again, this is especially important for SME contracts.[90]

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88. *Id.* arts. 10(5), 11(6) ("Where measures to verify compliance are carried out in relation to SMEs, the company shall bear the cost of the independent third-party verification. Where the SME requests to pay at least a part of the cost of the independent third-party verification, or in agreement with the company, that SME may share the results of such verification with other companies.").

89. This is a logical extension of the principle stated in Articles 10(1) and 11(1) that preventive and corrective measures must be designed to address both parties' contributions to the impact. *See id.* arts. 10(1), 11(1).

90. As concerns SMEs, they could be given a contractual choice: Establish and maintain their own due diligence process or participate in the buyer's due diligence process, noting that the latter option may be less onerous. This "opt out" provision could also be made available to larger business partners that are not in-scope for the CSDDD.

4. *Effectively Address Adverse Impacts*

A final method is for companies to include a contractual commitment to remediate adverse impacts as a matter of priority, ahead of order cancelations and termination. Commit to terminating the contract only as a last resort in the event of an adverse impact and to exit responsibly, not through "cut and run" or "zero tolerance" termination.

The CSDDD clearly states that disengagement for HREDD-related reasons should only be pursued as a last resort and only in case of *severe* adverse impacts where preventive or corrective action is unrealistic, meaning "there is no reasonable expectation that those efforts would succeed," or where such efforts have (definitively) failed.[91] Additionally, a company that is deciding whether to stay or go must do so responsibly, weighing whether the adverse impacts created by exit "can be reasonably expected to be manifestly more severe than the adverse impact that could not be prevented or adequately mitigated."[92] In such a case, the company may, at its discretion, continue the relationship. This language can fairly be read as creating an expectation that, if the company elects to disengage, it will first employ reasonably available measures to minimize the negative impacts of disengagement.

Disengagement is often not an appropriate measure for addressing (potential or actual) adverse impacts, as it does little to effectively prevent, minimize, correct, or remedy such impacts. Rather, it seeks to simply remove such impacts from the chain of activities, which will likely be inappropriate under the CSDDD. That being said, in some cases, particularly where

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91. *Id.* art. 10(6); *see also id.* art. 11(7). Articles 10(6) and 11(7), along with Recitals 50 and 57, provide that, for potential adverse impacts that could not be prevented or adequately mitigated, and for actual adverse impacts that could not be brought to an end or the impact of which could not be minimised by due diligence measures, "the company shall, as a last resort, be required to refrain from entering into new or extending existing relations with a business partner in connection with which, or in the chain of activities of which, the impact has arisen . . . ." *Id.* arts. 10(6), 11(7). Termination could be pursued for potential adverse impacts "if the implementation of the enhanced prevention action plan has failed to prevent or mitigate the adverse impact," *id.* art. 10(6), and, for actual adverse impacts "if the implementation of the enhanced corrective action plan fails to bring to an end or minimise the extent of the adverse impact . . . ." *Id.* art. 11(7). Even then, however, termination should only be "with respect to the activities concerned" and only if the "adverse impact is severe." *Id.* arts. 10(6), 11(7).

92. *Id.* art. 10(6)(b), 11(7)(b).

the supplier is clearly not willing to improve or cooperate, or where remaining in the contract (beyond a reasonable period of time) would cause additional severe impacts, severing the relationship may be necessary, also to send a signal that human rights and environmental concerns are taken seriously.

Furthermore, as explained above, contracts that allow for immediate suspension or termination in the event of adverse impacts are not appropriate because they reduce the likelihood that problems will be identified, disclosed, and addressed, let alone remediated. Furthermore, strict termination rights fail to meet the requirement that preventive and corrective measures must account for the buyer's own contributions to adverse impacts. In other words, if a buyer contributes to an adverse impact through, for example, their purchasing practices, that contribution would be erased—at least on paper—via an immediate termination clause that can only be invoked by the buyer.

Instead of immediate termination, "zero-tolerance" or "cut and run" clauses, contracts should include a clear procedure for addressing adverse impacts that may end in termination, but only as a last resort. The occurrence of an adverse impact should trigger a procedure where the parties work together to address the impact in question. The parties should contractually commit to providing HRE remediation in the shortest delay possible, including through the preparation and implementation, in consultation with adversely affected stakeholders, of (a) a preventive action plan to address potential adverse impacts or (b) a corrective action plan to address actual adverse impacts, in proportion to the parties' respective contributions to the impact(s).[93]

Including a clear remediation provision with a clear process for corrective action lessens the incentive for suppliers to hide problems because they will know, with contractual certainty, that there will be an opportunity to fix (cure) the problem in collaboration with their buyer(s).[94] The contract could also clarify that if it becomes clear that corrective efforts will fail

93. *Id.* recitals 50, 57.

94. The CSDDD says that in-scope companies must provide remediation (only) if they have caused or jointly caused an actual adverse impact; where a company did not cause or jointly cause an actual adverse impact, the Directive says that it may provide "voluntary remediation" and "use its ability to influence the business partner that is causing the adverse impact to provide remediation." *Id.* art. 12(1) and (2). To contractualize this requirement, we recommend that in-scope companies commit to providing assistance, guidance, and

(or have already failed), contractual sanctions, including suspension, penalties, and eventually, termination, may be exercised. Although it should only be invoked as a last resort, the right to terminate should be preserved in the contract as a preventive measure: It sends a strong signal that the company is serious about HREDD, which helps to deter misconduct by the counterparty.

Lastly, the contract should require that a party wishing to exit the contract must do so responsibly. The termination of a contract can lead to adverse impacts, for example, by affecting the capacity of the supplier to pay adequate living wages to their workers or to retain their workers. If the terminating party is in-scope, it must take measures to address these impacts.[95] Clarifying this expectation in the contract would better inform—and may even change—the decision to terminate. Measures for mitigating the impacts of termination vary; some examples include helping workers find new jobs, providing training to up-skill affected workers, and contributing to a severance fund. Such measures would limit the adverse impacts generated by termination, which under the CSDDD must not be unreasonable in comparison with the adverse impacts that led to termination.[96]

At a minimum, the party wishing to exit should provide reasonable notice to its counterparty and pay for outstanding invoices incurred prior to the termination date.[97] This will allow the partner to prepare for disengagement and to do their part to mitigate the impacts of termination, for example, by finding new customers. It will also help prevent the problem of workers not being paid for work already performed (wage theft),[98] which happened on a dramatic scale when buyers cancelled orders (even for goods that were completely manufactured and shipped) during the COVID-19 pandemic.[99]

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other support to facilitate the remediation process, as needed, regardless of whether they jointly caused the impact.

95. *Id.* art. 10(6)(b), 11(7)(b).

96. *Id.* recitals 50, 57.

97. *Id.* art. 10(6), 11(7).

98. *Id.* annex I § 1, No. 6 (specifically asks companies to ensure the payment of living wages).

99. Vogt et al., *Farce Majeure*, *supra* note 34, at 1; Ruggie & Sherman, *supra* note 15.

Conclusion

Due diligence-aligned contracts require the parties to set aside risk-shifting approaches and perfect compliance expectations in favor of a shared-responsibility approach. This represents a paradigm shift in how commercial contracts are designed, performed, and terminated. This article has explained how the CSDDD's requirements in relation to contracts could bring about such a paradigm shift. Contracts and codes of conduct will continue to play a critically important role in companies' implementation of due diligence within their supply chains, but companies will have to fundamentally change how they design these instruments to meet the CSDDD's appropriateness requirement. Companies should prepare for these new requirements and start reviewing and upgrading their contracts and codes accordingly. In making the transition toward due diligence-aligned contracting, companies would be well advised to integrate the shared-responsibility principles that are enshrined in the CSDDD, which is built on the foundation set by the UNGPs and the OECD standards.[100] The summary chart in the appendix captures the key Dos and Don'ts of due diligence-aligned contracting identified in this article. These Dos and Don'ts are reflected in the EMCs, the model clauses being developed by the European Working Group for Responsible and Sustainable Supply Chains consisting of European legal practitioners, academics, and business and human rights experts, including the authors of this article. The EMCs aim to contractualize the CSDDD requirements and provide a template for due diligence-aligned contracting that can be used not only to adhere to the legal requirements and meet responsible conduct standards, but also and more importantly, to improve the protection of workers and the environment across global supply chains. [101] Version 1.0 of the EMCs will be published in Fall 2025 on the RCP website.[102]

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100. For an analysis of the German Supply Chain Act yielding a similar conclusion, see Dadush, Schönfelder & Braun, *supra* note 15. *See also* Michaela Streibelt & Daniel Schönfelder, *Effective and Appropriate HREDD Requires a Shared Responsibility Approach, Responsible Contracting & Purchasing*, NOVA Centre on Bus., Hum. Rts. and the Env'n Blog (Nov. 8, 2023), https://novabhre.novalaw.unl.pt/effective-and-appropriate-hrdd-requires-a-shared-responsibility-approach-responsible-contracting-purchasing/.

101. *The European Model Clauses (EMCs)*, Responsible Contracting Project, https://www.responsiblecontracting.org/emcs.

102. *Id.*

A note regarding on-going legal developments: The CSDDD entered into force in July 2024, after protracted and contentious negotiations. In February 2025, the European Commission proposed a new bill referred to as the "Omnibus Bill" that, if passed, would change aspects of the CSDDD, the CSRD, and the EU Taxonomy Regulation.[103] According to the Commission, the purpose of the Omnibus is to simplify the rules promulgated under the European Green Deal and mitigate their effects on the EU's competitivity.[104] The Omnibus is still very much a work in progress and there is no way to know now what the final text will contain or indeed if there will even be a final text. Thus, until further notice, the CSDDD text analyzed above remains the law of the land. That said, the current draft of the Omnibus, if adopted, would affect some aspects of our analysis.

Most significant for contracts, the proposed Omnibus modifies the scope of the due diligence requirements. In-scope companies would still need to "take appropriate measures to identify and assess actual and potential adverse impacts arising from their own operations or those of their subsidiaries and, where related to their chains of activities, those of their business partners."[105] But, when it comes to carrying out in-depth assessments into the parts of their supply chain "where adverse impacts were identified to be most likely to occur and most severe," companies would be required to do that only with respect to their direct (tier 1) suppliers, not all their chain-of-activity partners involved in the high-risk corners of their supply chain.[106] In practice this would mean that only direct suppliers would be the focus of in-scope companies' HREDD-related

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103. Eur. Comm'n, *Proposal for a Directive of the European Parliament and of the Council amending Directives 2006/43/EC, 2013/34/EU, (EU) 2022/2464 and (EU) 2024/1760 as regards certain corporate sustainability reporting and due diligence requirements*, COM (2025) 81 final (Feb. 26, 2025) [hereinafter Omnibus], https://commission.europa.eu/document/download/1d14a487-f042-476f-997f-adf7c3e14950_en?filename=CSDDD%20Omnibus%20proposal.pdf.

104. For a Q&A on the Omnibus prepared by the Commission, see Eur. Comm'n, *Questions and answers on simplification omnibus I and II* (Feb. 25, 2025), https://ec.europa.eu/commission/presscorner/detail/en/qanda_25_615.

105. CSDDD, *supra* note 1, art. 8(1).

106. Omnibus, *supra* note 103, at 38. "Amendments to Directive [CSDDD] . . . Article 8 is amended as follows: (A) in paragraph 2, point (b), is replaced by the following: '(b) "based on the results of the mapping as referred to in point (a), *carry out and in-depth assessment of their own operations, those of their subsidiaries and, where related to their chains of activities, those of their direct business*

measures, which would pose a number of challenges for effectiveness that have been discussed elsewhere.[107] Softening this concern, however, is the caveat that "[w]here a company has *plausible information* that suggests that adverse impacts at the level of the operations of an indirect business partner have arisen or may arise, it shall carry out an in-depth assessment."[108] While the "plausible information" standard is vague, it does not sound like a particularly high bar. Information regarding product or supply chain risks that is made publicly available by, for example, the press, law firms, or NGOs, would likely qualify.[109] If this is correct, the effect of this new language on the scope of HREDD obligations may be limited.

Of note, while contracts are not included in Article 8 (Identifying and assessing actual and potential adverse impacts) of the CSDDD, the draft Omnibus would mention them there as well: "irrespective of whether plausible information is available about indirect business partners, a company *shall seek contractual assurances from a direct business partner that that business partner will ensure compliance with the company's code of conduct by establishing corresponding contractual assurances from its business partners.*"[110] If this language is adopted, it would likely increase the temptation for in-scope companies to risk-shift through their contracts. However, under the current proposal, the appropriateness criteria and the Recitals discussed above would not

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partners, in the areas where adverse impacts were identified to be most likely to occur and most severe.'" *Id.*

107. *See e.g.*, Daniel Schönfelder, *Lieferkettengesetz: Weniger Aufwand, mehr Wirkung*, Initiative Lieferkettengesetz (Mar. 14th, 2025), https://lieferkettengesetz.de/wp-content/uploads/2025/03/250320_Kurzgutachten_LkSG_Schoenfelder.pdf. (discussing the challenges suppliers face due to HREDD related measures).

108. Omnibus, *supra* note 103, at 38. Paragraph 2a is added to Article 8: "2a. *Where a company has plausible information that suggests that adverse impacts at the level of the operations of an indirect business partner have arisen or may arise, it shall carry out an in-depth assessment.*" *Id.*

109. *Id.* at 26. recital 21 says that "Plausible information means information of an objective character that allows the company to conclude that there is a reasonable likelihood that the information is true. This may be the case where the company concerned has received a complaint or is in the possession of information, for example through credible media or NGO reports, reports of recent incidents, or through recurring problems at certain locations about likely or actual harmful activities at the level of an indirect business partner. Where the company has such information, it should carry out an in-depth assessment." *Id.*

110. *Id.* at 38.

change; therefore, we expect risk-shifting contracts to remain inappropriate for compliance purposes. Should there be a more explicit requirement for companies to contractually "cascade"[111] HREDD obligations to ensure their direct business partners "follow"[112]—not comply perfectly with—their code of conduct and that their partners' partners do the same, then it will be even more important for companies to be vigilant about embedding shared responsibility principles in their contracts. Otherwise, companies could violate the Directive's non-transfer requirement. Vigilance should, as always, be heightened if and when SMEs are involved.

In sum, our view is that, should the Omnibus Bill be adopted as currently proposed, it would have little effect on our analysis concerning the content and form of due diligence-aligned contracts. If anything, the text would strengthen the argument for shared responsibility to avoid transferring obligations to business partners and achieve effective HREDD.

111. *Id.* at 26, recital 21 says that "companies should seek to ensure that their code of conduct – which is part of their due diligence policy and sets out the expectations as to how to protect human, including labour, rights and the environment in business operations – is *followed* throughout the chain of activities in accordance with *contractual cascading and SME support.*" (emphases added).

112. *Id.*

Appendix

Summary Chart: The dos and don'ts of CSDDD-aligned contracting

Dos	Don'ts
Share contractual responsibility for HREDD	Use contracts simply to transfer HREDD responsibilities and obligations to business partners
Commit to cooperate to address adverse impacts in an on-going, risk-based, and dynamic fashion to incentivize transparency and trust	Use contracts to establish one-sided (supplier-only) obligations on a strict liability basis where any imperfection is a breach + partners are incentivized to hide problems
Commit to responsible purchasing practices and fair commercial terms with all partners, but especially SMEs. Where possible, commit the seller to do the same with its sellers	Ignore the reality that the buyer's purchasing practices can contribute to, or jointly cause, and aggravate adverse impacts
Commit to fair commercial terms that can support effective HREDD	Use contracts to formalize unfair commercial terms that can aggravate adverse impacts
Ensure that HREDD-related costs are fairly distributed in the contract, based on the parties' respective capacities and resources. Ensure that business partners have the capacity and support needed to meet HREDD requirements. This is important for all partners, but especially SMEs.	Overwhelm suppliers with unreasonable HREDD expectations, obligations, and informational requirements (e.g., questionnaires, scorecards, reports)
Jointly prioritize human rights and environmental remediation over suspension, cancelation, and termination. Clarify termination is a last resort.	Aggravate the risk of adverse impacts via immediate (zero-tolerance) termination rights
Commit to exiting responsibly by giving reasonable notice and taking measures to mitigate the impacts of termination	"Cut and run" at the first sign of HREDD-related trouble

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COMMENTARY ON THE CSDDD AND CONTRACTS: A RESPONSE TO DADUSH, SCHÖNFELDER, AND STREIBELT

DAVID FRYDLINGER*

INTRODUCTION

I have been asked to comment on the excellent policy brief authored by Professor Sarah Dadush, Daniel Schönfelder and

* David Frydlinger is a Swedish attorney and partner at Cirio law firm in Stockholm. He regularly advices clients on matters of sustainable business law. He is the author and co-author of eight book, among them Frydlinger, D., Rules of the Game for Sustainable Business – Laws, Contracts and Morality, Wolters Kluwer, 2024, on EU sustainability law.

Michaela Streitbelt.[1] (I refer to the three of them hereinafter as "the authors".) Because I agree with most of what the authors argue—principally, that the CSDDD[2] (hereinafter used interchangeably with "the Directive") says about contracts—I will focus this comment on a fundamental theme brought forward by the policy brief: legal theory.

This is, first of all, a question about how the authors can arrive at their interpretation of the CSDDD. There are a few candidates for legal theories that they could have used. Legal positivism,[3] law and economics,[4] and interpretivist theory[5] have dominated the scene for the past fifty years or so, having varying influence and position in different jurisdictions. In this article, I claim that the authors can only have arrived at their interpretation under the interpretivist theory. I further claim that the authors are right in applying this theory because the interpretation of the CSDDD exposes the fundamental weaknesses of legal positivism and law and economics, not only as theories on interpreting a piece of sustainability law such as the CSDDD, but also any law.

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1. Dadush et al., *What Does the EU CSDDD Say About Contracts?*, 21 N.Y.U. J.L. & Bus. 245 (2025).

2. Directive (EU) 2024/1760 of the European Parliament and of the Council of 13 June 2024 on Corporate Sustainability Due Diligence, Amending Directive (EU) 2019/1937 and Regulation (EU) 2023/2859, 2024 O.J. (L 1760) 1.

3. For an overview of this theory, see, e.g., Patricia Mindus & Torben Spaak, Cambridge Companion to Legal Positivism (2021). The foremost representative of this theory of law is H.L.A. Hart. *See* H.L.A. Hart, The Concept of Law (2d ed. 2012). Another important, more contemporary representative is Joseph Raz. *See, e.g.*, Joseph Raz, Between Authority and Interpretation (2009).

4. The literature in law and economics is vast. For an overview, see, e.g., The Oxford Handbook of Law and Economics: Volume 1: Methodology and Concepts (Francesco Parisi ed., 2017). The foremost proponent of law and economics is probably Richard Posner. *See, e.g.*, Richard A. Posner, The Economic Analysis of Law (9th ed., 2014). Other important proponents are Ronald Coase and Guido Calabresi. *See, e.g.*, R. H. Coase, *The Problem of Social Costs*, 3 J.L. & Econ. (1960); *see also* Guido Calabresi, The Costs of Accidents: A Legal and Economic Analysis 135 (1970).

5. The foremost representative of interpretivism is Ronald Dworkin. *See, e.g.*, Ronald Dworkin, Taking Rights Seriously (2013); Ronald Dworkin, Law's Empire (1986); Ronald Dworkin, Justice for Hedgehogs (2011). Other proponents of interpretivism, different from Dworkin, are Mark Greenberg and Nicos Stavropoulos. *See, e.g.*, Mark Greenberg, *The Moral Impact Theory of Law*, 123 Yale L.J. 1288 (2014); Nicos Stavropoulos, *Interpretivist Theories of Law*, in Stanford Encyclopedia of Philosophy (Edward N. Zalta ed., 2021) (2003), https://plato.stanford.edu/entries/law-interpretivist/.

Some may ask, "Does theory matter?" I think it certainly does. Violations of the CSDDD can lead to obligations to pay damages[6] or penalties.[7] Legal positivism, law and economics, and interpretivism lead to different interpretations of CSDDD concepts such as appropriate measures[8] and due diligence,[9] so if not for other reasons, working under the best theory of interpretation should be good risk mitigation practice. But there is another, more profound, reason why theory matters. When studying and trying to interpret CSDDD and other acts of EU sustainability law, I have realized that the choice of legal theory is, in and of itself, a sustainability question—a point I will demonstrate in this article.

I.
The CSDD and Legal Theory

A key concept in the CSDDD is the concept of "appropriate measures," a requirement which the authors correctly argue both allows and limits companies' discretion in designing and carrying out human rights and environmental (hereinafter "HRE") due diligence. Article 3(1)(o) of the Directive defines this concept as "measures that are capable of achieving the objectives of due diligence by effectively addressing adverse impacts in a manner commensurate to the degree of severity and the likelihood of the adverse impact, and reasonably available to the company, taking into account the circumstances of the specific case, including the nature and extent of the adverse impact and relevant risk factors."[10]

Taking appropriate measures as a response to identified risks or actual cases of adverse effects on HRE is part of what it means to conduct business with "due diligence," which is the core (but undefined) concept of the Directive. As the authors point out, Articles 10 and 11 set out contracts as an instrument to take appropriate measures. The key question from a contractual perspective, as formulated by the authors, is then, "What is an appropriate, due diligence-aligned contract?"

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6. Directive (EU) 2024/1760, *supra* note 2, at Art. 29
7. *Id.* at Art. 27.
8. *Id.* at Art. 3.1 (o).
9. *Id.* at Art. 5.
10. *Id.* at Art. 3.1 (o).

The authors list seven "dos" and seven "don'ts" of CSDDD-aligned contracts, based on an interpretation of the CSDDD Articles and Recitals that relies on a legal theory.

I will begin by describing legal positivism, law and economics and legal interpretivism as candidates of the legal theory applied by the authors. Each of these legal theories are rich with many themes, nuances, and perspectives. However, I will not describe them in any detail. Instead, I will capture what I believe is the core of each theory, before moving on to analyze which of them the authors used and whether they, in my view, were right in doing so.

A. *Legal Positivism*

The core of legal positivism is that the law is a *historical fact*, which means that law cannot and should not be interpreted based on underlying moral principles.[11] To interpret the law means interpreting past decisions of legislators or courts, whose expressions of what the law is are viewed as authoritative under legal positivism. To determine which historical facts are also legal facts, legal positivism provides a theory based on a *rule of recognition*,[12] which is not a written rule, but a rule deduced from the social practice of judges and lawyers, showing what they *in fact* recognize as being the law, without recourse to what *should be* considered as being the law.

Under this theory of interpretation, an interpreter of CSDDD will have to pay very close attention to the texts of the Recitals and Articles of the Directive. To the largest extent possible, the concept of "appropriate measures" should be interpreted based on clear expressions and examples included in the texts of CSDDD.

B. *Law and Economics*

The law and economics theory shares some key characteristics with legal positivism but is also quite different. Both

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11. *See, e.g.*, Raz, *supra* note 3, at 10 ("[T]he content of the law can be established without resort to moral considerations bearing on the desirability or otherwise of any human conduct, or of having any particular legal standard. Moreover, the law CONSISTS of standards which are the product of human activity, largely of actions intended to impose duties, confer rights, and more generally to set binding standards.").

12. *See* HART, *supra* note 3, at 100.

theories view law as something empirical and not a product of an underlying moral order. But while legal positivism finds law in history, law and economics looks into the future. Its basic premise is that law is about generating *economic efficiency*.[13] In tort law, for example, law and economics would allocate liability for damages to the person or entity that could avoid the damage at the lowest cost.[14] In corporate law, law and economics dictates that business be run to maximize shareholder value as that would minimize transaction costs in the market.[15]

The key question is then, "What is economic efficiency?" Two basic tests have been developed over the years. A law is Pareto efficient when no one can be made better off without making someone else worse off.[16] Pareto efficiency is quite restrictive because it is most often the case that a law may be beneficial to the general good, while being detrimental to some. The law is thus not efficient under this criterion. A more practical criterion is therefore Kaldor-Hicks efficiency, which theorizes that a policy is efficient if the winners could compensate the losers and still be better off.[17] In simpler terms: Kaldor-Hicks efficiency looks at the net effects to society of a law. The interpretation that generates the most net positive effect is the correct interpretation, given that it is possible to compensate the losers.

Under this theory, the appropriate measures to mitigate risks of or eliminate actual cases of adverse HRE impacts is a matter of economic efficiency. An appropriate measure would then be a measure that finds the break-even point between the marginal costs for society avoided when the adverse impact is mitigated or eliminated and the marginal costs for implementing the measure.

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13. Robert Cooter & Thomas Ulen, Law and Economics 7 (6th ed. 2014).

14. *See, e.g.*, Calabresi, *supra* note 5.

15. *See, e.g.*, Reinier Kraakman et al., The Anatomy of Corporate Law: A Comparative and Functional Approach (3d ed. 2017).

16. *See* Cooter & Ulen, *supra* note 13, at 14; Posner, *supra* note 4, at 14.

17. This criterion was developed in parallel by the economists John Hicks and Nicholas Kaldor. *See* John R. Hicks, *The Foundations of Welfare Economics*, 49 Econ. J. 696, 712 (1939); Nicholas Kaldor, *Welfare Propositions in Economics and Interpersonal Comparisons of Utility*, 49 Econ. J. 549, 552 (1939).

C. *Legal Interpretivism*

Though there are other scholars in this school of thought, when addressing legal interpretivism, I refer to the legal theory of Ronald Dworkin.[18] The core of legal interpretivism is that all legal cases should be handled based on a consistent set of principles that *treat all citizens as equals.*[19] If legal positivism claims that lawyers look to historical events and law and economics claims that law should looks into the future, legal interpretivists look for an interpretation of the law that comes closest to treating all citizens as equals. Dworkin famously called this *law as integrity.*[20] The law consists of rules and principles, and the judges interpret the laws by trying to keep the system of rules and principles as consistent as possible. When doing this, the judge will unavoidably have to rely on some moral principles, such as freedom and equality. This is not only what judges actually do, but also what they should do.[21]

II.
What Legal Theory is Applied in the Brief?

A close reading of the policy brief indicates that the authors align very closely with legal positivist theory. The authors base their list of "dos" and "don'ts" on a close reading primarily of Articles 10 and 11, along with Recitals 45, 46 and 54 of the Directive.[22] Based on this reading, they list obligations not to employ risk-shifting contracts that simply transfer due diligence responsibilities on business partners and instead to include shared-responsibility clauses such as adjustment of purchasing practices where relevant, inclusion of cost sharing arrangements and so on.

However, an even closer reading shows that the authors are not strict positivists. They make claims about the CSDDD that are hard to derive directly from the legal texts. For example, the authors argue that contracts should be designed to reflect that

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18. *See, e.g.*, Dworkin, Taking Rights Seriously, *supra* note 5; Dworkin, Law's Empire, *supra* note 5; Dworkin, Justice for Hedgehogs, *supra* note 5. Other proponents of interpretivism include Mark Greenberg and Nicos Stavropoulos.
19. *See, e.g.*, Dworkin, Law's Empire, *supra* note 5, at 96.
20. *Id.* at 225.
21. Dworkin, Taking Rights Seriously, *supra* note 5, at 22.
22. Dadush et al., *supra* note 1, at 266–79.

purchasing practices is part of due diligence by "(a) identify responsible purchasing practices as a due diligence obligation and (b) including commitments to specific purchasing practices that are likely to be relevant for preventing the adverse impact in the supply chain at issue."[23] While I agree that this tracks CSDDD, the Directive does not include express language to this end. This and similar examples[24] show that the authors are not only exploring historical facts taking place in June 2024 when the Directive was adopted as required by legal positivism.

Furthermore, it is quite clear that the authors are not applying law and economics in their interpretation of the CSDDD. The text is completely silent on considerations of economic efficiency, which instead would have been in the forefront if law and economics had been applied.

I would argue that the authors of the policy brief are applying legal interpretivism. As already shown, the authors are not strictly positivists since they claim that CSDDD calls for, for example, contractual clauses regarding responsible procurement practices, something not explicitly stated in the Directive's text. Further the authors can only come to such a conclusion if they interpret CSDDD as expressing a set of principles, which not only give meaning to the explicit wording in the Directive, but also lead to obligations not explicitly laid out in the text (such as an obligation to include a responsible procurement practice clause in a supplier contract).

III.
Which Theory is Best when Interpreting the CSDDD?

Are the authors "right" in applying legal interpretivism? Is that the best theory to used when interpreting the CSDDD? I think so. To substantiate this, I will begin by making some preliminary remarks, and then I will try to show how unfit legal positivism and law and economics would be for interpreting the CSDDD.

The policy brief exposes a clear challenge of interpreting the CSDDD under legal positivism: the Directive's text points more to the *measures* than to what is *appropriate*. A contractual assurance to comply with a code of conduct for due diligence

23. *Id.* at 272.
24. *Id.* at 266–69 (recommending that one avoids strict liability clauses).

can be appropriate, but what must the content of the assurance be for these measures to be appropriate? A contract that shares the responsibility for due diligence may be an appropriate measure, but what division of responsibility meets the appropriateness standard? A positivist may, in response to the latter question, refer to Recital 45, which instructs that appropriate measures should take due account of the level of the company's involvement in the negative impact.[25] Using distinctions made in the OECD Guidelines and UNGPs, recital 45 notes the difference between direct cause, contribution and direct linkage to negative impacts. A legal positivist may prefer such formulations since they can qualify empirically and not morally how responsibilities should be allocated (by pointing to a simple cause-and-effect chain).

With legal positivism, a judge or lawyer will ultimately have to make a normative assessment of a measure and decide whether this measure is appropriate. However, CSDDD and the other legal or semi-legal instruments that the Directive refers to—for example, the UNGPs—do not contain explicit statements of norms and principles to be applied when making an assessment that would be sought for by the positivist.

Legal positivism would make it very hard to interpret the CSDDD in practice. When it comes to law and economics, the problems are more of a normative nature. The most common criticism of law and economics is that it does not consider distributional aspects of wealth. This means that the theory may recommend solutions that are unjust.[26] Simply put, a law can violate human rights but still meet the Kaldor-Hicks criterion for efficiency.[27] This obviously renders this theory unfit for

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25. *See* Directive (EU) 2024/1760, *supra* note 2, at Recital 45 ("[W]hen assessing the appropriate measures to prevent or adequately mitigate adverse impacts, due account should be taken of the so called 'level of involvement of the company in an adverse impact' in line with the international frameworks and the company's ability to influence the business partner causing or jointly causing the adverse impact.").

26. *See, e.g.*, RONALD DWORKIN, A MATTER OF PRINCIPLE 242 (1985).

27. The reason for this is the following: the Kaldor-Hicks criterion looks for the solution that generates the highest net gain for society. If there are winners and losers in a particular solution, for example winners in the form of a company building a factory and losers in the form of ingenious people being driven from their land, the law is efficient as long as (i) the company wins more from building the factory than the people whose human rights are violated lose, and (ii) the company can compensate the people for their loss. It is thus not important that they are in fact compensated; it is important is

interpreting CSDDD, which is about protecting those human rights.[28]

These preliminary remarks point to deeper flaws in both legal positivism and law and economics, which should be highlighted, thereby making it clear why legal interpretivism is the best theory to use when interpreting the CSDDD.

A. *The Effects of the "Training Effect"*

In a 2022 paper, Ash, Neidu and Chen examine the effects of the law and economics training program of the Manne Economics Institute for Federal Judges which trained U.S. federal judges in law and economics between 1976 and 1999.[29] The study analyzes whether attending this program influenced judicial behavior, particularly in relation to the use of economic language, the issuance of conservative rulings, and policy decisions.[30]

Ash, Neidu and Chen find that judges who attended the program increased their use of economic terminology in their opinions[31] and tended to rule more conservatively in economics-related cases.[32] Specifically, these judges were more likely to rule against regulatory agencies,[33] favor more lenient enforcement in antitrust cases, and impose longer criminal sentences.[34] The paper concludes that the law and economics movement, through its impact on judicial thinking, contributed to shifts in U.S. legal decision-making, influencing key aspects of economic policy.[35]

The paper is not the only one showing how training in economics tends to make people behave more like how economists already assume them to be,[36] but it is one of the few papers

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that they *can* do it. *See* Hicks, *supra* note 17 (introducing the compensation principle); Kaldor, *supra* note 17 (developing efficiency criteria in economic policy).

28. *See* Directive (EU) 2024/1760 *supra* note 2, at Annex, Part 1.

29. Elliott Ash et al., *Ideas Have Consequences: The Impact of Law and Economics on American Justice*, (Nat'l Bureau of Econ. Rsch., Working Paper No. 29788, 2022).

30. *Id.* at 2.

31. *Id.* at 25.

32. *Id.* at 28–31.

33. *Id.* at 31–33.

34. *Id.* at 33–42.

35. *Id.* at 51.

36. *See, e.g.*, Ariel Rubinstein, *A Skeptic's Comment on the Study of Economics*, 116 Econ. J. C3, C6, C9 (2006).

focusing on lawyers. Its conclusions seriously undermine both legal positivism and law and economics as interpretive theories applicable to CSDDD.

Neither legal positivism nor law and economics can, within their theoretical frameworks, address the fact that judges trained in law and economics begin to write and reason more in economic terms. Assuming my claim that the core of legal positivism is the view of law as historical facts is correct, it is obvious that training in law and economics is *not* a historical fact that should affect how the law is interpreted. The only relevant historical facts are decisions by the legislator and the courts. The fact that a group of judges underwent training in law and economics would and should not matter under legal positivism, because judges are understood only to look at historical facts.[37] But it did matter: trained judges altered their legal practices because of the training, and they started to interpret the laws based on theories, principles, and thought models that clearly do not stem from the legal system itself. Legal positivism simply fails at explaining what is going on in the court rooms.

Law and economics runs into even greater problems. Law and economics claims that legislators *in fact* adopt laws that optimize economic efficiency (typically under the Kaldor-Hicks criterion) and that judges *in fact* interpret the laws to the same end.[38] It is therefore impossible for law and economics to explain why judges trained in law and economics tend to act more like how they are already assumed to act. Law and economics has no theory about its own effect. It is, to use the language of moral philosopher Derek Parfit, "a self-defeating theory,"—one that fails based on its own premises.[39]

The troubles for law and economics go much further and show some fundamental paradoxes within. Most of law and economics is based on microeconomic theory,[40] including the

37. It could be argued that if a judge trained in law and economics makes a judgement based on its theories, then *that judgement* becomes an historical fact of relevance. The problem for positivism remains however, because the training effect should not, according to this theory, have entered the legal universe in the first place.

38. *See, e.g.*, Coase, *supra* note 4. Ronald Coase's famous article is a foundational text in law and economics that analyzes judgements in light of his transaction cost theory. *Id.* at 1, 8–15.

39. Derek Parfit, Reasons and Persons 3 (1984).

40. Cooter & Ulen, *supra* note 13, at 11.

fundamental economic theory of *expected utility*.[41] In simplified terms, this theory tries to explain all human behavior as an individual's attempt to optimize maximize their utility. In each situation, an individual has many choices of courses of action. Each choice is, accordingly, allocated a level of utility and a likelihood that this level of utility will be gained if that choice is made.[42] Expected utility theory holds that people act to maximize their expected utility, calculated as the product of level and likelihood.[43]

It has already been shown several times, not least within behavioral economics, that people in fact do not act according to expected utility theory.[44] The work of Kahneman and Tversky are of particular importance here. I would argue, however, that the fact that judges are affected by law and economics training shows not only the fundamental flaws of expected utility theory but also the irreconcilability of law and economics based on this theory.

The very act of setting up a training program in law and economics for judges is paradoxical since judges are assumed to behave in the way that the training is intended to train them into behaving. Furthermore, law and economics posits that people's actions in general are supposed to lead to economic efficiency given legal rules and judgements, but those who have not undergone training in economic theory will not act as expected utility theory predicts. This leads to the conclusion that law and economics cannot predict the effects of legal decisions contrary to what it suggests. Therefore, it should not be of particular use.

Legal positivists and legal and economic theorists could argue that even though they fail in explaining how legislators and judges *actually* behave, their normative recommendations on how they *should* behave still remain valuable. However, that

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41. *See, e.g.*, Paul Anand, Foundations of Rational Choice Under Risk (1993) (providing a deeper explanation of this theory). In law and economics, it is assumed that people are not only aiming to maximize their utility in economic matters, but in all parts of life. *See, e.g.*, Posner, *supra* note 4.

42. Cooter & Ulen, *supra* note 13, at 43–44.

43. *Id.*

44. *See, e.g.*, Daniel Kahneman & Amos Tversky, *Prospect Theory: An Analysis of Decision under Risk*, 47 Econometrica 263, 274 (1979); *see also* Christine Jolls, *Behavioral Economics and the Law*, 6 Founds. & Trends Microeconomics 173, 188–89 (2011); Richard H. Thaler, The Winner's Curse: Paradoxes and Anomalies of Economic Life 23 (1992).

argument would also be weak. A legal positivist would argue that judges *should only* consider historical legal facts when interpreting a law such as the CSDDD. Where would the normative force of such argument come from? The legal positivist, a law professor, for example, has two possible answers to this question depending on whether the law professor their statements on law as part of the valid rules of the legal system. If they think their statement is made outside of the legal system, it will result in absurdity because they will have to claim that judges *within* the legal system must pay no attention to what they are saying. If the professor instead believes that the statement about how a judge should rule is made *within* the legal system, that will lead to an infinite regress problem since it would be necessary to ask what rule gives authority to their statement and so on. A normative system cannot legitimize itself.

A law and economics theorist would argue that judges should interpret a law such as the CSDDD in a way to maximize economic efficiency. But this position would quickly run into unsolvable paradoxes hidden in the law and economics framework itself. Expected utility theory, the theory of behavior underlying law and economics, posits that the behavioral assumptions of the theory only apply given perfect market conditions, that is, the absence of market failures such as information asymmetries, negative externalities, or aggregation of market power by dominant players.[45] However, these are idealized conditions that never exist, despite the fact that a key idea of law and economics is that it is possible to generate those conditions through policies and laws.[46] This, here, is the paradox: law and economics must assume that market failures are the result of people acting according to expected utility theory, because that is the framework's only theory of human behavior.[47] This then leads to the conclusion that law and economics

45. *See, e.g.*, COOTER & ULEN, *supra* note 13, at 38–42 (examining market failures).

46. "As you can well imagine, this condition is unlikely to be realized in the real world." *Id.* at 38. The standard recommendations from law and economics are antitrust laws to combat monopoly and market power, subsidies or state provision to combat problems public goods problems, obligations to disclose information to combat asymmetries, and various forms of economic incentives (such as taxes) to combat externalities. *Id.* at 38–42.

47. I argue, therefore, that the famous Coase Theorem is seriously flawed, despite being fundamental in law and economics. Economist Ronald Coase argued that if transaction costs are low, people will be able to negotiate con-

must predict that training in expected utility theory and law and economics will generate the very market failures that law and economics suggest judges trained in law and economics can avoid. Therefore, a law and economics theorist arguing that judges *should* apply the law based on law and economics would thus be arguing for generating the very conditions of imperfect markets—including externalities such as human rights violations and environmental destruction—that the same theorist claims can be avoided by applying law and economics.[48]

B. *The Legal Interpretivist Path*

Thus far, the concept of "appropriate measures" in CSDDD is hard to interpret using a strictly positivist view. Nor does law

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tracts in the market that will generate socially efficient outcomes. Coase, *supra* note 4 at 15–17. But then Coase has two choices, depending on whether he assumes that expected utility theory applies even in imperfect markets. If so, he must assume that transaction costs are generated by actors behaving according to expected utility theory. However, transaction costs are a necessary consequence, both in practice and in theory. This means, for law and economics, that laws and judgements can never lower transaction costs.

Alternatively, if the theorem is limited to perfect market conditions, he can avoid this problem, but then the theorem becomes useless. What use is showing that something is perfect only under certain conditions? Law and economics is not only about understanding the world but improving it. If expected utility theory applies only to perfect market conditions, advising a judge (which is what a law and economist theory is giving) to analyze the law and make a judgement *as if* transaction costs are zero would be strange because the advisor has no idea why market conditions are imperfect, and therefore no basis to claim that such an analysis would, in fact, reduce transaction costs.

48. Law and economics theorists are of course not unaware of the problems with their theory. Richard Posner is explicit in his seminal book *The Economic Analysis of Law* that the underlying assumptions of the theory are unrealistic. His defense is, however, symptomatic of a broader problem. All theories, Posner contends, must be based on abstractions from a very complex reality, which by default will make them "unrealistic" in the sense that they do not fully capture the world they seek to describe. Posner, *supra* note 4, at 17. He refers to Isaac Newton's "unrealistic" speculation of how bodies would fall in vacuum as an example. But of course, Newton did not "extract" relevant pieces of information from a reality used to build a theory of this reality. He used mathematics to reconstruct and thereby explain the movement of bodies (i.e., the planets). Had Newton devised a theory of gravity, which by its own assumptions collapsed under scrutiny, that would not have been much of a theory. For a theory to be scientific, which Posner claims his theory to be, it must be logically consistent. Otherwise, it can hardly claim to provide a logically consistent explanation of what's going on in the world that the theory seeks to explain. *Id.*

and economics offer a viable alternative. As argued above, that theory could allow for or even generate the very violations of human rights that the Directive, among other things, intends to mitigate. This leads us to legal interpretivism.

As the authors point out, the appropriateness standard both allows for and limits companies' discretion.[49] This is due to the very fact that the standard is expressing a set of underlying principles that gives meaning to the entire legal act. I argue that these underlying principles all refer back to what Dworkin's concept of *human dignity*.[50] Dworkin does not refer to some higher moral order but instead to the moral principles expressed in national constitutions and international charters on human rights.[51] His argument is simple, but profound.[52] We humans have an *ethical* responsibility to live good lives.[53] This responsibility stands on two pillars: the principles of self-respect and authenticity.[54] Self-respect means that we have a responsibility to take our lives seriously and it is important how we live our lives; the principle of authenticity posits that to take our lives seriously is to identify what counts as success in our own lives, and we should not let others make those decisions for us.[55] Dignity requires us to live based on a coherent set of principles or values.

This has profound implications. If we accept that we are ethically obliged to show self-respect and authenticity for ourselves, we are, or so Dworkin argues, forced to acknowledge these principles for others as well.[56] The ethical principles regarding our duties toward ourselves translate into moral duties towards others. We must thus respect everyone's lives as important and let people define their own values to live by. This is the foundation to all human rights, where the right to life, privacy, freedom of thought, expression, and so on are just

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49. Dadush et al., *supra* note 1, at 265.
50. Dworkin, *supra* note 5, at 195.
51. *Id.* at 403, 405.
52. *Id.* at 202.
53. *Id.* at 196.
54. *Id.* at 203–04.
55. *Id.*
56. *Id.* at 260 ("Your reason for thinking it objectively important how your life goes is also a reason you have for thinking it important how anyone's life goes: you see the objective importance of your life mirrored in the objective importance of everyone else's."). Dworkin appears to imply a third principle, namely one of integrity. I argue that it is integrity that forces upon us the consistency necessary to respect others as we respect ourselves.

different manifestations of treating everyone with dignity. Since it is hard to live a life with dignity as defined by Dworkin if the conditions are undermined by climate change or other forms of environmental destruction, such forms of environmental destruction are fundamentally violations of peoples' dignity.

This has several implications. First, under legal interpretivism, what makes a measure such as a contract *appropriate* under CSDDD ultimately depends on whether the measure protects human rights by, for example, creating proper working conditions, affording fair salaries, avoiding emissions, and so on. Put another way, the principles of human dignity as expressed through human rights provide the basis for interpreting what is appropriate.

The second implication is that the question of legal theory is also a question of sustainability. Sustainability, or sustainable business, requires running businesses with the respect for those affected by the businesses. Legal positivism and law and economics are not compatible with this construct of sustainability. A legal positivist could argue that an interpretation of the "appropriate measures" concept considering human rights is consistent with the positivist theory because those human rights have been parts of the legal system. But how can a positivist interpret what those human rights stand for in, for example, a contract, without applying principles from outside the legal system that give meaning to those human rights? The problems of law and economics should also be obvious. A theory that, if applied, will allow or even generate violations of human rights and environmental destruction is not compatible with the requirements of sustainability. In sum, the academic struggle regarding legal interpretation theory is also a sustainability struggle.

The third implication relates to contracts, particularly what CSDDD says about contracts. In the next section, I will focus on answering the question as formulated by the authors, "What is an appropriate, due diligence-aligned contract?"

IV.
Legal Interpretivism and Contracts in CSDDD

Assume that only an interpretivist interpretation of CSDDD can be correct. What implication does this have for what CSDDD says about contracts and the authors' arguments? First, this means that CSDDD is saying both more *and* less about contracts

than what the authors claim with their list of seven do's and seven "don'ts". CSDDD is saying *more* because the principles of human dignity underlying the appropriateness standard have further practical implications for contracts than those in the authors' list. CSDDD is saying *less* because some of the "dos" and "don'ts" in the authors' list apply only in certain situations where the principles of human dignity so require. This list of "dos" and "don'ts" could be made both longer and shorter. The authors do not claim that their list is exhaustive, so I am certain they would agree.

Appropriate measures such as contracting must, according to Articles 10 and 11 of the Directive, only be taken when risks of or actual adverse impact have been identified. As the authors point out, to be appropriate, the measures must be effective, in the sense that they must reasonably lead to prevention or elimination of the adverse impact. It is important to note, however, that appropriateness is not only an *empirical* but also a *normative* concept. The policy brief could have made this point more explicitly. A measure like a contractual assurance is empirical because it must be grounded in reality and the companies' cause-and-effect chains to prevent or eliminate the impact. But this is not sufficient. From an empirical perspective, a company could in theory prevent or eliminate adverse impact by, for example, obliging a supplier to take all responsibility for the adverse impact—basically outsourcing its due diligence obligations. While, as the authors point out, such one-sided behavior can inadvertently worsen the adverse impacts, this is not always the case. It is possible to think of scenarios where one-sided obligations could still produce the intended effects of preventing or eliminate adverse impacts: a one-sided obligation on a supplier to stop using non-sustainable material, for example.

But, as the authors correctly point out, companies may not outsource their due diligence obligations, even if outsourcing could have been effective. Recital 46 of the Directive notes that contractual assurances should be designed to ensure that responsibilities are shared appropriately by the company and its business partners. While such sharing is not always necessary to prevent or eliminate an adverse impact, the Directive still requires so, because Articles 10 and 11 (where the obligations regarding contractual assurances are expressed) should be interpreted in light of Recital 46. This is what I refer to as the *normative* aspect of the appropriateness standard. In other

words, it is not only important to empirically prevent or eliminate the adverse impact. *How* it is done also matters.

From an interpretivist perspective, this makes perfect sense. Taking appropriate measures is a part of acting with due diligence, which is the core norm of the Directive. If a company would contribute to the usage of child labor in the supply chain through its price pressuring procurement practices and would then have its tier-one supplier along with all sub-suppliers address this issue without the company's involvement, that would in itself be a violation of CSDDD's due diligence norm.[57]

This means that for a measure to be appropriate, it is not sufficient that it is effective. It must also not violate the basic due diligence norm. This norm is expressed in Article 5 of the Directive as systematic behaviors that companies must demonstrate.[58] The norm should be based on policies, be integrated into risk management systems and involve identification, prevention, elimination and remediation of damages resulting from adverse impacts. This fulfills the requirement of respecting the principles of human dignity when carrying out business under the interpretivist framework.

Assuming this is correct, it raises some interesting questions about how far the Directive's requirement on contracts reaches. If appropriateness means not only being effective but also following the due diligence norm, then arguably an appropriate, due diligence-aligned contract is a contract that is not the result of and does not lead to violations of human dignity. This is the basis of my claim that the authors' "dos" and "don'ts" list in the policy brief is both too long and too short. As an example: Sharing of the costs for due diligence, which is on the list, can certainly be appropriate. But it could also be appropriate to have only one of the parties carry those costs if the other party takes on a corresponding burden somewhere else in the contract. On the other hand, the list could also have only one don't: a prohibition on violating human dignity through your contracts. Said another way, act with due diligence. The list could also include many more points, all of which

57. In a supply chain, the tier-one supplier is the supplier directly contracting with the customer. The tier-two supplier is the sub-supplier contracting with the tier-one supplier, and so on.

58. *See* Directive (EU) 2024/1760, *supra* note 2, art. 5.

would be further examples of the same human dignity principle. I trust the authors would agree with me on this.[59]

If a due diligence-aligned contract under CSDDD is a contract that does not violate the principles of human dignity, this means that the parties must be equal able to make autonomous decisions uninfluenced by the bargaining power of a stronger party during the very process of entering into the contract and the allocation of responsibilities and risks in the contract. It would also mean that neither party should have unilateral rights—unilateral termination rights, for example—unless such unilaterality compensates for an underlying imbalance between the parties.

Conclusion

I will end my comment with a question. Professor Ian Macneil famously drew a distinction between transactional and relational contracts.[60] Transactional contracts are formal, short-term agreements with precise terms, focusing on legal enforceability and specific exchanges. They are rigid with little room for flexibility once agreed upon.[61] In contrast, relational contracts emphasize long-term relationships, trust, and cooperation. These agreements are less formal and more flexible, relying on mutual understanding and the ability to adapt to

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59. Articles 10.5 and 11.5 state that when contractual assurances are obtained from small and medium-sized enterprises (SMEs), the terms must be fair, reasonable and non-discriminatory. Directive 2024/1790, *supra* note 2, arts. 10, 11. These interesting paragraphs raise an important question: do contractual assurances *not* have to be fair, reasonable, and non-discriminatory they are obtained from a large company? I highly doubt that the authors would hold such view. All contracting lawyers know that many terms in contracts between large companies are not fair, reasonable, or non-discriminatory. One-sided risk shifting which risks generating incentives for actions detrimental to human rights and the environment can and does occur between large companies, who only partly derive their bargaining power from size. Therefore, the only plausible interpretation of these articles can be that contractual assurances with SMEs must *always* be fair, reasonable and non-discriminatory, regardless of whether they would otherwise qualify as an appropriate measure. This means that such assurances must still be fair, reasonable and non-discriminatory between large companies, only that the appropriateness standard applies in specific cases.

60. Ian R. Macneil, *The Many Futures of Contracts*, 47 S. Cal. L. Rev. 691, 720–25 (1974).

61. Ian Macneil, The Relational Theory of Contract: Selected Works of Ian Macneil 185 (2001).

changing circumstances. They are designed to nurture ongoing partnerships.[62]

I have, with the co-authors, tried to increase the use of relational contracts.[63] In my latest book on EU sustainability law, I try to make a case for relational contracts to improve sustainability in supply chains.[64] In the conclusion of the policy brief, the authors note that "CSDDD's requirements in relation to contracts may well bring about a paradigm shift in how commercial contracts are designed, performed, and terminated."[65] The focus in the CSDDD on shared responsibilities and cooperation to deal with adverse impacts certainly align very closely with the relational contract model. The obvious question, then is whether the CSDDD bring about a paradigm shift towards an increased use of relational contracts.

62. *Id.* at 186.

63. *See, e.g.*, David Frydlinger et. al., *A New Approach to Contracts*, Harv. Bus. Rev., Sep.–Oct. 2019; David Frydlinger et. al., Contracting in the New Economy: Using Relational Contracts to Boost Trust and Collaboration in Strategic Business Relationships (2021).

64. David Frydlinger, Rules of the Game for Sustainable Business: Laws, Contracts and Morality (2024).

65. I think that Professor Dadush would agree that this paradigm shift can be described by using the distinction between "extractive" and "pro-social" contracts she makes in a 2022 article. *See* Sarah Dadush, *Prosocial Contracts: Making Relational Contracts More Relational*, 85 L. & Contemp. Probs. 153 (2022).