Response to the Commission’s Consultation Document Proposal for an Initiative on Sustainable Corporate Governance

8 February 2021

INTRODUCTION

As negative consequences of climate change and environmental degradation become increasingly visible, the immense threat that we are faced with if we continue business as usual, is no longer deniable. Despite a broad consensus on the need for responsible business conduct, respect of human rights and preventing environmental harm, widespread environmental harm and violations of human rights demonstrate that voluntary initiatives are ineffective. Therefore, we applaud the European Commission for considering a proposal aimed to address these major challenges.

The implementation of the EU Sustainable Finance agenda continues. The Platform on Sustainable Finance is working on further developing the EU Taxonomy1 aimed at facilitating sustainable investment by including social and governance dimensions as well as defining environmentally negative and low impact activities. We are also expecting proposals aiming at improving availability, comparability and quality of corporate sustainability-related disclosures.

These are all welcomed and needed initiatives. Improved ESG corporate disclosures are necessary to enable investors to take informed decisions and channel financial flows needed for the transition and green recovery. However, disclosure alone is not sufficient to meet the level of ambition set by the EU Green Deal and EU’s 2050 net-zero greenhouse gas emissions target. To achieve those objectives, we need to change corporate behaviour and ensure that sustainability considerations are truly embedded within companies and their governance including their strategies, decision-making and oversight.

SUMMARY of KEY PROPOSALS

Directors duties

- We need an EU framework specifying directors’2 duty to act in the company’s long-term interest while taking into account broader stakeholder interests – moving away from the ‘shareholder primacy’ or ‘profit maximization model’ to a stakeholder-focused economic model.

- Corporate directors should be responsible for:
  - Ensuring that sustainability risks and adverse sustainability impacts on the environment and society are properly identified and integrated into the company’s strategy.
  - Setting and adopting measurable sustainability targets (including short, medium and long-term targets) and a transitional pathway / plan to meet those targets. Sustainability targets should be aligned with the EU’s net zero and other EU sustainability goals.

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1 Regulation (EU) 2020/852 on the establishment of a framework to facilitate sustainable investment

2 Throughout this paper we are referring to both executive and non-executive directors following a definition in Art. 2 (i) of the Shareholder Rights Directive (Directive 2007/36/EC).
- Monitoring the implementation of the transition plans and meeting sustainability targets.
- Overseeing the company’s due diligence process.

- Setting the right incentives can be a powerful tool to encourage certain behaviours and corporate decisions. We therefore strongly suggest to align corporate directors’ pay with sustainability targets (50% of variable remuneration). The remaining 50% of directors’ variable remuneration could be linked to financial performance of the company. However, we suggest to limit strictly the alignment of directors’ remuneration with the share price as share price movements often do not reflect the evolution of the intrinsic company value and can distract directors’ attention from sustainable value creation.

- Directors should aim to achieve gender balance on the board and gender representation reflecting the situation of the overall company on the executive committee (if a company’s employees are 65% women (men), then the executive committee should be composed of 65% of female (male) members.

- Effective enforcement, including dissuasive sanctions and directors’ personal liability, is needed.

**Due diligence**

Voluntary initiatives on due diligence requirements, even when supplemented by transparency requirements, fall short of ensuring responsible business conduct, respect for human rights and corporate accountability for the impact of business activities on society and the environment.

The study conducted for the European Commission demonstrates that only one in three businesses claims to undertake a due diligence process taking into account all human rights and environmental impacts. This is not enough considering how many companies destroy the environment, abuse workers’ and basic human rights, remove indigenous people off their land or even accept, or benefit from modern days slavery. Evidence also shows that those who stand up to corporate abuses are often fired from their jobs, and in some countries persecuted or worse.

The EU should assume leadership in this area and put forward a proposal for an ambitious EU legal framework for environmental and human rights due diligence in corporate operations and global value chains. Given the insufficient effectiveness of voluntary or disclosure-based initiatives, this framework should hold businesses accountable when a lack of compliance with the due diligence process has led to harm people or the environment.

To that end, among the Commission’s proposals, we support an approach providing for minimum processes and definitions which would:

- Result in a minimum set of requirements regarding the processes which should be applicable across all sectors.
- Provide harmonised definitions for example as regards the coverage of adverse impacts that should be the subject of due diligence obligations and should rely on the UN and the OECD guidelines and the ILO conventions.
- Be complemented with further requirements, in particular for environmental issues.
- Where necessary, be supplemented by a guidance and sector specific rules complementing the due diligence duty.

Directors should be responsible for an oversight of the company’s due diligence process as part of their duty of care. Effective enforcement, including dissuasive sanctions and judicial enforcement with liability and compensation in case of harm caused by not fulfilling the due diligence obligations, will be key to ensure effectiveness of the rules.

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3 Throughout this paper we are referring to both executive and non-executive directors following a definition in Art. 2 (i) of the Shareholder Rights Directive (Directive 2007/36/EC).

4 [https://op.europa.eu/en/publication-detail/-/publication/8ba0a8fd-4c83-11ea-b8b7-01aa75ed71a1/language-en](https://op.europa.eu/en/publication-detail/-/publication/8ba0a8fd-4c83-11ea-b8b7-01aa75ed71a1/language-en)
RESPONSES TO SPECIFIC QUESTIONS

Section I: Need and objectives for EU intervention on sustainable corporate governance

Questions 1 and 2 below which seek views on the need and objectives for EU action have already largely been included in the public consultation on the Renewed Sustainable Finance Strategy earlier in 2020. The Commission is currently analysing those replies. In order to reach the broadest range of stakeholders possible, those questions are now again included in the present consultation also taking into account the two studies on due diligence requirements through the supply chain as well as directors’ duties and sustainable corporate governance.

Question 1: Due regard for stakeholder interests’, such as the interests of employees, customers, etc., is expected of companies. In recent years, interests have expanded to include issues such as human rights violations, environmental pollution and climate change. Do you think companies and their directors should take account of these interests in corporate decisions alongside financial interests of shareholders, beyond what is currently required by EU law?

☒ Yes, a more holistic approach should favour the maximisation of social, environmental, as well as economic/financial performance.
☐ Yes, as these issues are relevant to the financial performance of the company in the long term.
☐ No, companies and their directors should not take account of these sorts of interests.
☐ Do not know.

Please provide reasons for your answer:

Corporate purpose and its impact on the society and environment have been increasingly debated in recent years. Various scandals and investigations have shown that companies often make financial profits at the expense of employees working in suboptimal or even unacceptable conditions, customers interests and to the detriment of the environment, whilst negative environmental impacts are neither accounted nor paid for. In many instances, the main beneficiaries of these profits are company directors and management as well as shareholders with short-term objectives, in a context where short-term share price trends are not necessarily in line with the company’s long-term interest and development. Data shows¹ the increasingly growing pay-gap between executive / directors’ and average employees’ remuneration, while investment in R&D tends to decrease.

Europe will not be able to meet its goal of climate neutrality by 2050 unless we change the way businesses are run. It is high time we move away from the “shareholder primacy”, the model that has been predominant for decades, to a “stakeholder-focused economic model” where the purpose of the corporation is sustainable value creation rather than purely economic profitability.

There seems to be a growing support for such a model, including among business leaders. In 2019, 181 CEOs of Business Roundtable, including America’s largest corporations, declared¹ that companies should serve not only their shareholders, but also deliver value to their customers, invest in employees, deal fairly with suppliers and support the communities in which they operate.

In its resolution² of 17 December 2020, the European Parliament stressed that “companies are not abstract entities detached from today’s environmental and social challenges” and that “their long-term performance, resilience and even their survival may depend on the adequacy of their response to environmental and social matters”.

Indeed, consideration and integration of sustainability risks and adverse environmental and social impacts
in corporate decision-making and strategy is in the long-term interest of all companies. This is particularly obvious regarding sustainability risks as they these are understood as environmental, social or governance events or conditions that, if they occur, could cause an actual or a potential material negative financial impact for the company. Meanwhile, the adverse sustainability impacts are understood as negative environmental and social impacts of companies’ operations. However, adverse sustainability impacts can eventually pose sustainability risks to the company’s operations. For instance, wild fires, flooding, water scarcity or even social unrest due to a health-related crisis can eventually have a major impact on a company’s operations and its financial results.

That is why companies must consider all stakeholders’ interests, including those of employees, customers and society at large, and shall consider and address sustainability risks and social and environmental impacts of their business. Of course, this is not straightforward and it may take time to develop the necessary methods and models to support corporate decision making.

Definitions of ‘director’ vary. For the purpose of this consultation, we presume that the Commission’s understanding of directors is aligned with the definition in the Shareholder Rights Directive:

(i) any member of the administrative, management or supervisory bodies of a company;

(ii) where they are not members of the administrative, management or supervisory bodies of a company, the chief executive officer and, if such function exists in a company, the deputy chief executive officer;

(iii) where so determined by a Member State, other persons who perform functions similar to those performed under point (i) or (ii).

In short, we understand that questions in the consultation document refer to both executive and non-executive direction, including top management.

2 https://purpose.businessroundtable.org/

Question 2: Human rights, social and environmental due diligence requires companies to put in place continuous processes to identify risks and adverse impacts on human rights, health and safety and environment and prevent, mitigate and account for such risks and impacts in their operations and through their value chain.

In the survey conducted in the context of the study on due diligence requirements through the supply chain, a broad range of respondents expressed their preference for a policy change, with an overall preference for establishing a mandatory duty at EU level.

Do you think that an EU legal framework for supply chain due diligence to address adverse impacts on human rights and environmental issues should be developed?

☒ Yes, an EU legal framework is needed.
☐ No, it should be enough to focus on asking companies to follow existing guidelines and standards.
☐ No action is necessary.
☐ Do not know.

Please explain:

We strongly believe that there is a need for an EU regulatory action for a mandatory framework on human rights, social and environmental due diligence in companies’ operations and through their value chain.
As recognised by the European Parliament in its report\(^1\) on sustainable corporate governance of December 2020, and by the study\(^2\) carried out for the European Commission by the London School of Economics, CIVIC consulting and British Institute of International and Comparative Law, the existing voluntary initiatives promoting due diligence requirements have not proven sufficiently effective in changing corporate behaviour.

The study demonstrates that only 37% of the businesses surveyed claim that they currently undertake some form of due diligence covering human rights and environmental impacts. Meanwhile, only about 16% cover the entire value chain. Remarkably, these numbers include companies which are already subject to due diligence legislation due to requirements at national level (e.g. France).

These results are broadly aligned with several other recent surveys on the same topic. A recent survey\(^3\) by the German government concludes that only a small minority of companies address human rights and environmental abuses linked to their global business operations in the absence of mandatory requirements obligations. Only 460 out of 3 300 companies surveyed\(^4\), responded to the first round of the survey (2019). Out of these, only between 17% and 19% were able to document that they are duly performing human rights due diligence. Only 22% of companies surveyed\(^5\) were considered compliant with HRDD requirements during the second round of the survey running from March to May 2020.

The Danish Institute for Human Rights recently performed an assessment\(^6\) that shows that 20 of the biggest Danish companies are not demonstrating full alignment with the duty to respect human rights, as defined by the UNGPs, while 14 out of 20 score below 50%.

Analysis\(^7\) by the Alliance for Corporate Transparency shows that only 22.2% of 1000 companies analysed report on human rights due diligence processes and only 6.9% refer to their commitment to provide remedy for harmed people. While the focus of this study was on corporate reporting, it gives an indication of the number of companies actually undertaking human rights due diligence.

In the absence of mandatory rules, only a few well-intended companies set high standards for business conduct and strive for a sustainable corporate performance in consideration of the environment and society. In many cases, these businesses are at a competitive disadvantage towards companies that prioritise short-term profit over respect for human rights and the environment.

In the context of the current social and economic COVID-induced crisis as well as the looming climate emergency, it is more important and urgent than ever to require companies to put in place continuous processes to identify, assess, prevent and mitigate risks and adverse impacts on human rights, social matters and the environment in their operations and through their value chain. Companies should be also held accountable in case of harm caused by not fulfilling the due diligence obligations.

Some countries have already taken the steps in this direction (e.g., France with the duty of care / due diligence legislation). However, a patchwork of national legislation may jeopardise the single market and increase costs for businesses. A binding initiative at global level would be ideal to ensure an internationally consistent approach and to prevent multinational companies escaping the requirements. However, given the low likelihood of an agreement for introducing a legally-binding instrument to regulate the activities of multinationals at a global level, we do not see a realistic solution to this situation at the moment.

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\(^2\) https://op.europa.eu/en/publication-detail/-/publication/8ba0a8fd-4c85-11ea-bb87-01aa75ed71a1/language-en
\(^3\) https://www.auwaertiges-amt.de/de/aussenpolitik/themen/ausserwirtschaft/wirtschaft-und-menschenrechte/monitoringnap/2131054
\(^4\) https://lieferket tengesetz.de/Pressemitteilungen/DeutscheUnternehmen-Bi-45-46/Mensch-rechts-Test-durchgefallen-Katastrophen-Ergebnis-MachtLiegferkettengesetz-unumgaenglich
\(^5\) https://lieferkettengesetz.de/Pressemitteilung/stellungnahme-zur-menschenrechts-befragung-deutscher-unternehmen
\(^6\) https://www.humanrights.dk/sites/humanrights.dk/files/media/document/-%2003/345-60%20Documenting%20Business%20Respect%20for%20Human%20Rights%202020%200504132_1_1.pdf
\(^7\) https://www.alliancelforporatetransparency.org/assets/2019_Research_Report%20Alliance_for_Corporate_Transparency7d9802a0c18c9f13017d686481bd2d6c6886fead9e9c7a5c3cfafaea8a48b1c7.pdf
Question 3: If you think that an EU legal framework should be developed, please indicate which among the following possible benefits of an EU due diligence duty is important for you (tick the box/multiple choice)?

☒ Ensuring that the company is aware of its adverse human rights, social and environmental impacts and risks related to human rights violations other social issues and the environment and that it is in a better position to mitigate these risks and impacts
☒ Contribute effectively to a more sustainable development, including in non-EU countries
☒ Levelling the playing field, avoiding that some companies freeride on the efforts of others
☒ Increasing legal certainty about how companies should tackle their impacts, including in their value chain
☐ A non-negotiable standard would help companies increase their leverage in the value chain
☐ Harmonisation to avoid fragmentation in the EU, as emerging national laws are different
☐ SMEs would have better chances to be part of EU supply chains
☒ Other, please specify:

Findings of the OECD study “Quantifying the Costs, Benefits and Risks of Due Diligence for Responsible Business Conduct” (June 2016)¹ show that companies applying a comprehensive due diligence tend to outperform other companies on capital markets, enjoy increased shareholder returns, a stable share price, and improved investor satisfaction. Regarding human resources, companies performing due diligence have a greater ability to attract and retain talent, experience reduced turnover and hence lower recruitment and training costs, and enjoy a better reputation.


Question 3a. Drawbacks

Please indicate which among the following possible risks/drawbacks linked to the introduction of an EU due diligence duty are more important for you (tick the box/multiple choice)?

☐ Increased administrative costs and procedural burden
☐ Penalisation of smaller companies with fewer resources
☐ Competitive disadvantage vis-à-vis third country companies not subject to a similar duty
☐ Responsibility for damages that the EU company cannot control
☐ Decreased attention to core corporate activities which might lead to increased turnover of employees and negative stock performance
☐ Difficulty for buyers to find suitable suppliers which may cause lock-in effects (e.g. exclusivity period/no shop clause) and have also negative impact on business performance of suppliers
☐ Disengagement from risky markets, which might be detrimental for local economies
☒ Other, please specify:

The above-mentioned risks are frequently used by corporate lobbyists, yet they are largely exaggerated claims. Introducing a European mandatory due diligence legislation based on the UN Guiding Principles on Business and Human Rights and the OECD Due Diligence Guidance for Responsible Business Conduct would help mitigate these risks and keep the additional costs at a negligible level.
Moreover, due diligence is a tool that will help companies to identify, consider and mitigate the sustainability risks and adverse impacts which can negatively impact their business model and operations. In the current context of the looming climate crisis and upcoming major regulatory changes that will affect corporate business models, due diligence should become a basic risk assessment tool. All those elements being considered, it can be argued that the claim that mandatory due diligence framework would result in additional administrative burdens is not only questionable, but also of secondary importance.

With regard to the alleged risk of **penalisation of smaller companies**, the UN Guiding Principles on Business & Human Rights state that the means through which SMEs are expected to meet their responsibility to respect human rights and the environment should depend on human rights and environmental risk, but are also expected to be **proportional to their size**.

The due diligence study(1) done for the Commission demonstrates that, even for SMEs, the costs of carrying out mandatory supply chain due diligence appears to be relatively low compared to the company's revenue. The additional recurrent company-level costs are estimated **below 0.14% of companies' revenues** in case of SMEs.

Regarding the **alleged risk of responsibility for damages that EU companies cannot control**, it is essential to bear in mind that, under well-established civil liability principles, there would need to be a strong link between the harm and the company’s actions or its omissions as well as a certain level of control or influence of the company over the relevant subsidiary or business partner, to hold a company accountable.

Regarding the **alleged risks of decreased attention to core corporate activities** which might lead to **increased turnover of employees and negative stock performance and of disengagement from risky markets**, we find it surprising that these poor business lobby excuses aimed at defending the status quo are mentioned in the consultation paper.

To the contrary, findings of the OECD study "Quantifying the Costs, Benefits and Risks of Due Diligence for Responsible Business Conduct" (June 2016)(2) demonstrate that comprehensive due diligence is linked with outperformance in stock price, increased shareholder returns, reduced volatility and improved investor satisfaction. Regarding human resources, companies performing due diligence have a greater ability to attract and retain talent, experience reduced turnover and hence lower recruitment and training costs, and enjoy a better reputation.

The UN Guiding Principles on Business and Human Rights, the OECD Guidelines for multinational enterprises and the OECD Due Diligence Guidance suggest that companies should only consider ceasing relationships where options for leverage to prevent or mitigate negative impacts have been exhausted or leverage is insufficient.

Last but not least, could sever breaches of human rights or major environmental damages seriously be justified due to the administrative burden stemming from due diligence? When companies cannot find the resources to perform robust due diligence through their value chain, they should simply not pursue business opportunities with counterparties in the areas or countries which are known for human and labour
Section II: Directors’ duty of care – stakeholders’ interests

In all Member States the current legal framework provides that a company director is required to act in the interest of the company (duty of care). However, in most Member States the law does not clearly define what this means. Lack of clarity arguably contributes to short-termism and to a narrow interpretation of the duty of care as requiring a focus predominantly on shareholders’ financial interests. It may also lead to a disregard of stakeholders’ interests, despite the fact that those stakeholders may also contribute to the long term success, resilience and viability of the company.

Question 5. Which of the following interests do you see as relevant for the long-term success and resilience of the company?

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<th>Interest</th>
<th>Relevant</th>
<th>Not relevant</th>
<th>I do not know/I do not take position</th>
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<tr>
<td>the interests of shareholders</td>
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<td>the interests of employees</td>
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<td>the interests of employees in the company’s supply chain</td>
<td>X</td>
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<td>the interests of customers</td>
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<td>the interests of persons and communities affected by the operations of the company</td>
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<td>the interests of persons and communities affected by the company’s supply chain</td>
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As widely recognised by academic literature and corporate governance specialists, businesses do not operate in isolation from their environment. In its report of 2016 on Corporate governance for South Africa¹, King IV emphasised that companies need to consider the triple context of economy, society and environment and their governing bodies need to take account of the legitimate and reasonable needs, interests and expectations of all material stakeholders the execution of their duties in the best interests of the organisation over time.

In its recent resolution², the European Parliament stated that “companies are not abstract entities detached from today’s environmental and social challenges” and that “their long-term performance, resilience and even their survival may depend on the adequacy of their response to environmental and social matters”.

Corporate operations have an impact on the environment and society, which is usually not accounted for, not valued and not included in the prices of products or services. The natural resources, health and wellbeing of employees, customers, and communities is often taken for granted and treated as a free good that corporates can benefit from. However, various recent reports, including IPCC Special Report³ and IPEBES⁴ report, demonstrate that if we continue business as usual, the world we know will collapse soon and that societies and businesses will face an unprecedented climate and environmental disaster.

Therefore, we no longer have time for business as usual and we need to fundamentally change how corporations operate. As we are running out of time, a swift and strict regulatory intervention is necessary to ensure that businesses take responsibility and mitigate their impact on society and the environment.

Importantly, corporate negative impacts on the environment and society will eventually turn into sustainability risks with material financial impacts on businesses. Companies are affected by climate change, environmental degradation and societal challenges which can lead to major disruptions and social unrest.

The ongoing Corona virus crisis has demonstrated the major impact that a sustainability crisis can have on businesses and on the economy. That is why in the latest regulatory developments, EU policy makers require businesses to consider both sustainability risks on business and finance as well as the adverse impacts that business operations and investment decisions can have on the environment and society.

⁴ https://ipbes.net/global-assessment
other interests, please specify:

In addition to the interests of employees in the company’s supply chain and the interests of persons and communities affected by the company’s supply chain, the interests of suppliers are also important for the long-term success and resilience of the company. Partnerships based on trust and mutual respect are a foundation of sustainable and resilient supply chains and of the economy at large. Such an approach promotes sustainable economic growth.

**Question 6.** Do you consider that corporate directors should be required by law to (1) identify the company’s stakeholders and their interests, (2) to manage the risks for the company in relation to stakeholders and their interests, including on the long run (3) and to identify the opportunities arising from promoting stakeholders’ interests?

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<thead>
<tr>
<th>Identification of the company’s stakeholders and their interests</th>
<th>I strongly agree</th>
<th>I agree to some extent</th>
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<th>Management of the risks for the company in relation to stakeholders and their interests, including on the long run</th>
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<th>Identification of the opportunities arising from promoting stakeholders’ interests</th>
<th>I strongly agree</th>
<th>I agree to some extent</th>
<th>I disagree to some extent</th>
<th>I strongly disagree</th>
<th>I do not know</th>
<th>I do not take position</th>
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**Please explain:**

As explained in our responses to questions 1 and 5, companies must consider all stakeholders’ interests, including those of employees, customers and society at large, and shall consider and address sustainability risks and social and environmental impacts of their business.

The current directors’ duty to act in the best interest of the company has not resulted in identification and/or due consideration of sustainability risks and impacts on people and the planet by companies. Given the urgency to address the issue of climate change as well as to manage sustainability risks that companies are faced with, it is necessary to clarify that as part of their duty of care, directors must
consider stakeholders’ interests, both from the perspective of respecting legitimate interests of stakeholders, and from the perspective of the management of risks and opportunities.

Consideration of sustainability matters, given their great importance and impact, should be considered at a strategic level and properly embedded within corporate strategy. The responsibility to consult and engage with stakeholders, which will be also part of the corporate’s due diligence duty, must be therefore embedded throughout the corporate structure, and not rest solely with the board of directors. It should be clarified that directors are responsible to provide oversight over the quality of the company’s due diligence, and ensure that its results are integrated in the corporate strategy. That would ensure that the sustainability matters are duly considered at a strategic level, and that there is a transparency concerning their integration in the company’s overall strategy that facilitates meaningful engagement of investors and stakeholders.

The responsibility to consult and engage with stakeholders should be part of the process of identification, consideration and addressing of sustainability risks and adverse impacts. It should be also part of the corporate’s due diligence duty.

**Question 7.** Do you believe that corporate directors should be required by law to set up adequate procedures and where relevant, measurable (science–based) targets to ensure that possible risks and adverse impacts on stakeholders, ie. human rights, social, health and environmental impacts are identified, prevented and addressed?

☑️ I strongly agree
☐ I agree to some extent
☐ I disagree to some extent
☐ I strongly disagree
☐ I do not know
☐ I do not take position

**Please explain:**

We fully agree that corporate directors should be required to set up adequate procedures and measurable targets that, in the case of environmental matters and to the extent possible, should be science–based. Such procedures are essential to ensure that possible risks and adverse impacts on stakeholders, ie. human rights, social, health and environmental impacts are identified, prevented and addressed.

In view of the looming climate crisis and the EU's goal to achieve 2050 climate neutrality, companies should fundamentally transform how they do business. To achieve that, sustainability risks and adverse social and environment impacts should be addressed at a strategic level and fully embedded within the corporate strategy.

Measurable sustainability targets, ideally to be aligned with the EU climate and environmental goals, are essential to prevent window dressing and greenwashing and set clear corporate objectives. Those targets should be broken down into short, medium and long-term targets and directors should ensure that companies establish transitional pathway / plan to meet those targets. Directors should monitor the implementation of the transition plans and achievement of the sustainability targets.
50% of directors’ remuneration should be aligned with the corporate sustainability targets to ensure that incentives are aligned with corporate sustainability goals.

It is crucial that sustainability risks and adverse impacts are not only identified and disclosed, but that they are effectively managed. Setting specific targets is of great importance as measuring will be an important part of an efficient management process.

Identification and consideration of sustainability risks and adverse social and environmental impacts is closely linked with corporate due diligence obligations. Due diligence can play an important role in identification of sustainability risks and impacts and should be considered an integral part of incorporating sustainability in corporate governance. Therefore, the upcoming initiative should consider the role that directors must play to ensure that the corporate due diligence obligations are embedded throughout the corporate operations and strategies.

To ensure the effectiveness of this process, we suggest to clarify that the company is responsible for carrying out due diligence, as part of its operations, throughout the value chain and that directors shall be responsible for overseeing the implementation of the due diligence processes by the company and for ensuring that the company takes appropriate actions.

**Question 8.** Do you believe that corporate directors should balance the interests of all stakeholders, instead of focusing on the short-term financial interests of shareholders, and that this should be clarified in legislation as part of directors’ duty of care?

☐ I strongly agree  
☐ I agree to some extent  
☐ I disagree to some extent  
☐ I strongly disagree  
☐ I do not know  
☐ I do not take position

Please provide an explanation or comment

Businesses do not operate in isolation from their environment. Corporate operations have an impact on the environment and society, which is usually not accounted for, not valued and not included in the prices of products or services. At the same time, businesses are also affected by climate change, environmental degradation and the functioning of society at large (including social disruption and unrest). Adverse impacts on the environment and society eventually become sustainability risks with material financial implications on business. Please see our response to questions 5 for more detailed explanations.

Therefore, there is a need for clarifying directors' duties to act in the long-term interest of the company in consideration of stakeholder interests and business impacts on the environment and society.

**Question 9.** Which risks do you see, if any, should the directors’ duty of care be spelled out in law as described in question 8?
We see the risks of the rules being too generic / not precise enough. The study\(^1\) on directors’ duties and sustainable corporate governance performed by EY Italy for the European Commission shows that in all of the 12 jurisdictions researched, the legal frameworks already oblige directors to act in the company’s interest. In some jurisdictions, companies are also required to consider broader stakeholder interests. Lack of precision, e.g., regarding what is meant by company’s interest, combined with short-term market and shareholder pressures are seen as contributing to undue focus on short-term financial performance and growing shareholder payouts.

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\(^1\) https://op.europa.eu/en/publication-detail/-/publication/e47928a2-d20b-11ea-adf7-01aa75ed71a1/language-en

How could these possible risks be mitigated? Please explain.

We recommend to clearly specify that company directors have the duty to:

- Act in the **company’s long-terms interest** while **taking into account interest of various stakeholders** (including employees, customers, and local communities) and **considering the company’s impact on the environment and society**.

- Ensure companies design and implement **a robust due diligence** to **identify, assess and mitigate sustainability risks** on their business and **adverse impacts** of their business model and their operations on the environment and society.

- **Fully integrate sustainability considerations in the corporate strategy supported by measurable sustainability targets**. This should be complemented with an implementation plan with key milestones to reach the goals.

**Directors should be personally liable** for any breaches of the duty of care. Rules should be complemented with an effective enforcement, including dissuasive sanction and possibility to effectively seek redress before the courts in case of serious harm.

Where directors widely integrate stakeholder interest into their decisions already today, did this gather support from shareholders as well? Please explain.

Shareholder support for increased consideration of broader stakeholder interests has been growing as it leads to better resilience and improved long-term financial performance.

Investor groups like the UN Principles for Responsible Investment and the Investors Alliance for Human Rights have been calling for stronger public policies in this regard. Climate Action 100+ is a grouping of 500 investors with over US$47 trillion under management who pledged to engage with systemically important greenhouse gas emitters and other companies across the global economy that have significant opportunities to drive the clean energy transition with the aim of helping to achieve the goals of the Paris Agreement.

Growing investors’ support for increased consideration of broader stakeholders' interest is reflected by a growing number of climate-related, environmental and human rights due diligence resolutions.\(^1\)
Question 10. As companies often do not have a strategic orientation on sustainability risks, impacts and opportunities, as referred to in question 6 and 7, do you believe that such considerations should be integrated into the company’s strategy, decisions and oversight within the company?

☒ I strongly agree
☐ I agree to some extent
☐ I disagree to some extent
☐ I strongly disagree
☐ I do not know
☐ I do not take position

Please explain:

Properly addressing sustainability risks, opportunities and adverse impacts may require strategic decisions including transformation of the business model and hence should be addressed at a strategic level. To enable sustainable value creation, sustainability risks, opportunities and impacts on the environment and society should be fully integrated into the corporate strategy.

Directors should be responsible for overseeing the process and approving the strategy including the measurable sustainability targets. Directors should also monitor implementation of the strategy and of the transition plans. For more details see our response to questions 6-9.

Enforcement of directors’ duty of care

Today, enforcement of directors’ duty of care is largely limited to possible intervention by the board of directors, the supervisory board (where such a separate board exists) and the general meeting of shareholders. This has arguably contributed to a narrow understanding of the duty of care according to which directors are required to act predominantly in the short-term financial interests of shareholders. In addition, currently, action to enforce directors’ duties is rare in all Member States.

Question 11. Are you aware of cases where certain stakeholders or groups (such as shareholders representing a certain percentage of voting rights, employees, civil society organisations or others) acted to enforce the directors’ duty of care on behalf of the company? How many cases? In which Member States? Which stakeholders? What was the outcome?

Please describe examples:

Corporate law in the EU Member States does not properly equip stakeholders, especially those other than shareholders, to enforce the directors’ duty of care on behalf of the company. As pointed out by the
Commission’s study\(^1\) on directors’ duties, “the enforcement of company’s claims against directors for an alleged violation of the duty of care is problematic”. The study points out that “in most EU jurisdiction, the only actors empowered to instigate legal proceedings against the directors on behalf of the company are the board of directors, the supervisory board (in two-tier systems), and/or the shareholders in the general meeting.” The study highlights that the enforcement of the company’s claims against its directors faces two major problems: conflict of interest (obvious in the case of one-tier board structure, where the board brings the company’s claim against one of its own members) and the difficulties connected to collective legal action by shareholders. The study concludes that, due to these obstacles, enforcement levels are currently low in all Member States.

Taking this opportunity, we would like to point out that shareholders may use engagement and exercise their rights to put pressure on company directors. However, that requires a lot of resources, active cooperation among company shareholders and an alignment of their objectives. Moreover, shareholders face many hurdles on their way to exercise their rights.

Last year, a group of 11 investors filed a shareholder resolution at the AGM of Total to push the company to set targets for emission reductions. Despite a major cooperation of powerful investors, the resolution was rejected by 83% of votes cast ‘against’ compared to 17% ‘for’. Nevertheless, this action was seen by co-filing investors as positive given it sent a “strong signal” to the company’s management and board.

Regarding enforcement of directors’ duties by other stakeholders, currently this is very difficult or even impossible. In recent years, some charities became shareholders of some large American companies to put pressure on corporate boards especially regarding establishing and reporting on human rights due diligence process in operations and supply chain. To our knowledge none of these resolutions were passed. What’s more, some companies actually tried to block them.

Investors have been making efforts to require companies to implement human rights due diligence for several years. For instance, in 2015 SumOfUs filed a shareholder resolution urging the board of directors of Amazon to introduce a human rights risk assessment. The board of directors recommended that shareholders vote against the proposal.\(^2\)

Ahead of its 2019 AGM, Amazon managed to successfully block a resolution by Oxfam America and other co-filers. The resolution was asking the board to “commit to conducting and making available to shareholders Human Rights Impact Assessment for at least three food products Amazon sells that present high risk of adverse human rights impacts”. Legal counsel acting on behalf of Amazon argued that the company was entitled to exclude the proposal on the basis that it is irrelevant to the Company’s business and that it deals with Amazon’s ordinary business operations. Amazon reached out to the Securities Exchange Commission that concluded\(^3\) that “the proposal would micromanage the Company by seeking to impose specific methods for implementing complex policies in place of the ongoing judgments of management as overseen by its board of directors.”

Despite having successfully blocked Oxfam America’s resolution, in 2019, Amazon had 11 shareholder resolutions at its AGM, including on climate change.\(^4\) None of those resolutions were adopted.

Oxfam America and co-filers’ resolution was eventually admitted to a vote at the 2020 virtual AGM\(^5\). It was not adopted but received 30% support.\(^6\) It could be considered a success but it also shows how little influence shareholders of companies with dispersed ownership have, including with regard to holding directors’ accountable.
Question 12. What was the effect of such enforcement rights/actions? Did it give rise to case law? was it followed by other cases? If not, why?

Please describe:

Please see our response to question 11.

Question 13. Do you consider that stakeholders, such as for example employees, the environment or people affected by the operations of the company as represented by civil society organisations should be given a role in the enforcement of directors’ duty of care?

☒ I strongly agree
☐ I agree to some extent
☐ I disagree to some extent
☐ I strongly disagree
☐ I do not know
☐ I do not take position

Please explain your answer:

Directors should be personally legally liable for duty of care breaches. Rules should be complemented by effective enforcement, including dissuasive sanction and possibility to seek redress before the courts in case of serious harm. All stakeholders should be able to seek redress on reasonable grounds.

Question 13a: In case you consider that stakeholders should be involved in the enforcement of the duty of care, please explain which stakeholders should play a role in your view and how.

Section III: Due diligence duty

For the purposes of this consultation, “due diligence duty” refers to a legal requirement for companies to establish and implement adequate processes with a view to prevent, mitigate and account for human rights
(including labour rights and working conditions), health and environmental impacts, including relating to climate change, both in the company’s own operations and in the company’s the supply chain. “Supply chain” is understood within the broad definition of a company’s “business relationships” and includes subsidiaries as well as suppliers and subcontractors. The company is expected to make reasonable efforts for example with respect to identifying suppliers and subcontractors. Furthermore, due diligence is inherently risk-based, proportionate and context specific. This implies that the extent of implementing actions should depend on the risks of adverse impacts the company is possibly causing, contributing to or should foresee.

**Question 14:** Please explain whether you agree with this definition and provide reasons for your answer.

We agree with this definition. However, in order to make the process as rigorous as possible, we suggest to capitalize on existing international due diligence standards (the OECD Due Diligence Guidance for Responsible Business Conduct, the OECD Guidelines for multinational enterprises and the UN Guiding Principles on Business and Human Rights). In particular, we suggest to:

- Clarify that the aim is to respect human rights, the environment and good governance within a company’s own operations and global value chains.

- Specify that companies should first be required to effectively identify and assess actual or potential adverse human rights, environmental and governance impacts which they may cause, contribute to or be directly linked to either through their own activities or as a result of their business relationships.

- Require companies to track and monitor the implementation and effectiveness of the adopted measures. The results of these tracking and monitoring processes must be used to inform possible changes to the global business operations and human rights and environmental due diligence process.

- When the enterprise identifies that it has caused or contributed to actual adverse impacts, address such impacts by providing for or cooperating in their remediation.

We suggest to refer to the company’s “global value chain” instead of “supply chain”. While the former refers to all interrelated activities by which a company adds value to a product or services, “supply chain” may be more narrowly defined as referring to the production and distribution of a commodity. It should be also emphasised we are referring to the companies’ “global value chain”.

**Question 15:** Please indicate your preference as regards the content of such possible corporate due diligence duty (tick the box, only one answer possible). Please note that all approaches are meant to rely on existing due diligence standards, such as the OECD guidance on due diligence or the UNGPs. Please note that Option 1, 2 and 3 are horizontal i.e. cross-sectorial and cross thematic, covering human rights, social and environmental matters. They are mutually exclusive. Option 4 and 5 are not horizontal, but theme or sector-specific approaches. Such theme specific or sectorial approaches can be combined with a horizontal approach (see question 15a). If you are in favour of a combination of a horizontal approach with a theme or sector specific approach, you are requested to choose one horizontal approach (Option 1, 2 or 3) in this question.

☐ Option 1. “Principles-based approach”: A general due diligence duty based on key process requirements (such as for example identification and assessment of risks, evaluation of the operations and of the supply
chain, risk and impact mitigation actions, alert mechanism, evaluation of the effectiveness of measures, grievance mechanism, etc.) should be defined at EU level regarding identification, prevention and mitigation of relevant human rights, social and environmental risks and negative impact. These should be applicable across all sectors. This could be complemented by EU level general or sector specific guidance or rules, where necessary.

☐ Option 2. “Minimum process and definitions approach”: The EU should define a minimum set of requirements with regard to the necessary processes (see in option 1) which should be applicable across all sectors. Furthermore, this approach would provide harmonised definitions for example as regards the coverage of adverse impacts that should be the subject of the due diligence obligation and could rely on EU and international human rights conventions, including ILO labour conventions, or other conventions, where relevant. Minimum requirements could be complemented by sector specific guidance or further rules, where necessary.

☒ Option 3. “Minimum process and definitions approach as presented in Option 2 complemented with further requirements in particular for environmental issues”. This approach would largely encompass what is included in option 2 but would complement it as regards, in particular, environmental issues. It could require alignment with the goals of international treaties and conventions based on the agreement of scientific communities, where relevant and where they exist, on certain key environmental sustainability matters, such as for example the 2050 climate neutrality objective, or the net zero biodiversity loss objective and could reflect also EU goals. Further guidance and sector specific rules could complement the due diligence duty, where necessary.

☐ Option 4 “Sector-specific approach”: The EU should continue focusing on adopting due diligence requirements for key sectors only.

☐ Option 5 "Thematic approach": The EU should focus on certain key themes only, such as for example slavery or child labour.

☐ None of the above, please specify

Question 15a: If you have chosen option 1, 2 or 3 in Question 15 and you are in favour of combining a horizontal approach with a theme or sector specific approach, please explain which horizontal approach should be combined with regulation of which theme or sector?

We believe that the legal framework should define a minimum set of requirements with regard to the necessary processes which should apply to companies across all sectors, with regard to human rights, including labour rights, and environmental issues, including climate change.

The framework should allow for additional guidance or sector specific rules especially when they pose high human rights and environmental risk. Any sector-specific legislation should supplement, but not limit, the development and implementation of the proposed general legislation. This is in line with the OECD framework, providing both for a general and sector specific guidance.

Question 15b: Please provide explanations as regards your preferred option, including whether it would bring the necessary legal certainty and whether complementary guidance would also be necessary.
We believe that Option 3 would result in a level playing field across the EU, avoiding the creation of a patchwork of diverging national due diligence laws. That would be helpful especially to companies that have cross-border operations. Moreover, it would provide clarity and legal certainty for companies on the way they should implement the rules.

If a principles-based approach is followed (as per option 1), there is a risk of the rules being substantially watered down during the transposition in the Member States. It would also leave room for companies to do window-dressing and greenwashing.

Moreover, in recent years EU rules have been evolving into an ambitious framework on sustainable finance. The Regulation (EU) 2019/2088 on sustainability-related disclosures in the financial services sector (SFDR) has already introduced certain due diligence-related requirements. Financial market participants (FMPs) with more than 500 employees will need to consider principle adverse impacts of their investment decisions and publish a statement on due diligence policies with respect to those impacts. Recently published draft level 2 measures¹, specify indicators that FMPs will need to disclose. To make those rules work in practice, it is necessary to require that all companies perform due diligence with regard to environmental, social and governance matters and disclose the information necessary to evaluate it. This should include information which will be required to disclose against the indicators in SFDR.

We strongly believe that the EU framework on due diligence should not be restricted to human rights but cover all potential or actual adverse impacts on the environment, social and governance matters. Consideration of environmental impacts is of particular importance to meet the EU goal of climate neutrality by 2050. Moreover, human rights and the environment are deeply linked and interconnected. It could be argued that access to e.g. clean water and clear air are basic human rights.


**Question 15c:** If you ticked options 2) or 3) in Question 15 please indicate which areas should be covered in a possible due diligence requirement (tick the box, multiple choice)

☒ Human rights, including fundamental labour rights and working conditions (such as occupational health and safety, decent wages and working hours)
☒ Interests of local communities, indigenous peoples’ rights, and rights of vulnerable groups
☒ Climate change mitigation
☒ Natural capital, including biodiversity loss; land degradation; ecosystems degradation, air, soil and water pollution (including through disposal of chemicals); efficient use of resources and raw materials; hazardous substances and waste
☐ Other, please specify

**Question 15d:** If you ticked option 2) in Question 15 and with a view to creating legal certainty, clarity and ensuring a level playing field, what definitions regarding adverse impacts should be set at EU level?

NA
**Question 15e:** If you ticked option 3) in Question 15, and with a view to creating legal certainty, clarity and ensuring a level playing field, what substantial requirements regarding human rights, social and environmental performance (e.g. prohibited conducts, requirement of achieving a certain performance/target by a certain date for specific environmental issues, where relevant, etc.) should be set at EU level with respect to the issues mentioned in 15c?

We believe that this requires proper consideration as the effectiveness of the due diligence duty will largely depend on the robustness of the criteria and ‘performance standards’ against which the due diligence should be conducted.

In terms of human and labour rights, we suggest to refer to the OECD Guidelines for Multinational Enterprises, OECD Due Diligence Guidance for Responsible Business Conduct, UN Guiding Principles on Business and Human Rights, the declaration on Fundamental Principles and Rights at Work of the International Labour Organisation (ILO), the eight fundamental conventions of the ILO and the International Bill of Human Rights.

Regarding environmental aspects, we advise to refer to the OECD Guidelines for Multinational Enterprises and OECD Due Diligence Guidance for Responsible Business Conduct. Once the EU Taxonomy for ‘negative and low impact activities’ is developed, we suggest that it should become the reference benchmark of environmental adverse impacts.

**Question 16:** How could companies’- in particular smaller ones’- burden be reduced with respect to due diligence? Please indicate the most effective options (tick the box, multiple choice possible)

This question is being asked in addition to question 48 of the Consultation on the Renewed Sustainable Finance Strategy, the answers to which the Commission is currently analysing.

☐ All SMEs should be excluded
☐ SMEs should be excluded with some exceptions (e.g. most risky sectors or other)
☐ Micro and small sized enterprises (less than 50 people employed) should be excluded
☐ Micro-enterprises (less than 10 people employed) should be excluded
☒ SMEs should be subject to lighter requirements (“principles-based” or “minimum process and definitions” approaches as indicated in Question 15)
☒ SMEs should have lighter reporting requirements
☒ Capacity building support, including funding
☒ Detailed non-binding guidelines catering for the needs of SMEs in particular
☒ Toolbox/dedicated national helpdesk for companies to translate due diligence criteria into business practices
☐ Other option, please specify
☐ None of these options should be pursued

Please explain your choice, if necessary

All companies, regardless of size, should be required to conduct human rights and environmental due diligence. SMEs can also contribute to or cause adverse environmental impacts and / or human rights or labour law breaches. This is in line with the UN Guiding Principles on Business & Human Rights and
OECD Guidelines for Multinational Enterprises. However, as highlighted in those standards, the type of policies and processes expected should depend on their capacity.

SMEs value chains tend to be shorter and simpler. SMEs tend to have fewer suppliers and customers, which enables deeper and better-quality relationships. Therefore, due diligence in their own operations and value chain should be easier to perform. Studies demonstrate that the cost of compliance is typically related to the size of the enterprise. The Commission’s study (1) on due diligence requirements through the supply chain shows that, even for SMEs, the costs of carrying out mandatory supply chain due diligence appears to be relatively low compared to the company’s revenue. The additional recurrent company-level costs, as percentages of companies’ revenues, amount to less than 0.14% for SMEs.

While keeping the above-mentioned in mind, following the principle of proportionality, we suggest that SMEs would be subject to simpler rules, including simplified reporting requirements. Moreover, we suggest to support SMEs especially during the initial years of the new obligations. Capacity building could include support in a form of funding, toolbox/dedicated national helpdesk for companies to translate due diligence criteria into business practices and detailed non-binding guidelines catering for the needs of SMEs.

1 https://op.europa.eu/en/publication-detail/-/publication/8ba0a8fd-4c83-11ea-b8b7-01aa75ed71a1/language-en

Question 17: In your view, should the due diligence rules apply also to certain third country companies which are not established in the EU but carry out (certain) activities in the EU?

☒ Yes
☐ No
☐ I do not know

Question 17a: What link should be required to make these companies subject to those obligations and how (e.g. what activities should be in the EU, could it be linked to certain turnover generated in the EU, other)? Please specify.

We suggest that third country companies entering the EU single market to sell products or services should be required to follow the European due diligence rules. This would help spread the good practice further outside of the EU and create a better level playing field between EU and non-EU companies. There are already cases of EU rules extra-territorial obligations: Timber Regulation EU 995/2010 and Directive 2019/633 on unfair trading practices in business-to-business relationships.

Question 17b: Please also explain what kind of obligations could be imposed on these companies and how they would be enforced.

Non-EU companies selling products or services in the EU should be required to respect human rights and the environment, in their own operations, global value chains, and to undertake human rights and environmental due diligence for the products, services that are placed or activities undertaken in the EU.

Similarly to EU companies, aforementioned companies shall be also liable for any human rights abuses and environmental harm in their operations or value chains (without prejudice to other subcontracting and supply chain liability frameworks).

Robust enforcement, with effective sanctions, should be established to ensure that requirements are complied with.
**Question 18:** Should the EU due diligence duty be accompanied by other measures to foster more level playing field between EU and third country companies?

- ☐ Yes
- ☐ No
- ☒ I do not know

Please explain:

An international treaty regulating the activities of transnational corporations would be an ideal solution. However, given the low likelihood of an agreement for introducing a legally-binding instrument to regulate the activities of multinationals at a global level, we do not see a realistic solution to this situation at the moment.

**Question 19: Enforcement of the due diligence duty**

**Question 19a:** If a mandatory due diligence duty is to be introduced, it should be accompanied by an enforcement mechanism to make it effective. In your view, which of the following mechanisms would be the most appropriate one(s) to enforce the possible obligation (tick the box, multiple choice)?

- ☒ Judicial enforcement with liability and compensation in case of harm caused by not fulfilling the due diligence obligations
- ☐ Supervision by competent national authorities based on complaints (and/or reporting, where relevant) about non-compliance with setting up and implementing due diligence measures, etc. with effective sanctions (such as for example fines)
- ☐ Supervision by competent national authorities (option 2) with a mechanism of EU cooperation/coordination to ensure consistency throughout the EU
- ☐ Other, please specify

Please provide explanation:

EU law should provide for a legal liability for human rights and environmental harms that a company, or any company that they control or have the ability to control has caused or contributed to by not fulfilling the due diligence obligations. Judicial enforcement with liability and compensation in case of harm caused by not fulfilling the due diligence obligations is necessary to make companies accountable and ensure victims have a possibility to seek effective remedy for harm done.

**Question 19b:** In case you have experience with cases or Court proceedings in which the liability of a European company was at stake with respect to human rights or environmental harm caused by its subsidiary or supply chain partner located in a third country, did you encounter or do you have information about difficulties to get access to remedy that have arisen?

- ☒ Yes
- ☐ No

In case you answered yes, please indicate what type of difficulties you have encountered or have information about:
Victims of corporate abuse often face legal, procedural and practical obstacles while seeking justice vis-à-vis European companies where harm was caused by its subsidiaries or supply chain partners located in a third country.

On 11 September 2012, there was a fire in the Ali Enterprise garment factory in Karachi, Pakistan. Due to poor fire safety measures, workers were uninformed and eventually trapped by the fire. 258 workers died and hundreds were seriously hurt. At the time, KIK, a German retailer, was the factory’s main client. Victims brought a case to the German court, but the case was dismissed as, following Pakistani law, the statute of limitation had expired and the claimants were too late to seek justice.

In the 1980s, Boliden paid Promel to export industrial waste to Chile, where Promel disposed of the waste without removing the arsenic. This caused awful health effects, including cancers and neurological disorders, for people living near the site. In 2013 victims tried to address that by holding Boliden accountable in the Swedish courts, pleading that Boliden breached a duty to ensure that the sludge was appropriately processed by Promel. Following an appeal, in March 2019, the court dismissed the appeal ruling that the claim for damages had been filed too late while the cause of action was time-barred. Boliden has not faced legal consequences for this negligence.

Shell has been polluting the Niger Delta in Nigeria. Pollution caused by the activities of its subsidiary SPDC has caused major harm to the ecosystem and impacted most negatively local populations. Victims tried to seek redress before the Dutch courts. It took more than a decade to obtain the ruling (https://www.bloomberg.com/news/articles/2021-01-29/dutch-court-orders-shell-nigeria-to-compensate-for-oil-spills). The court’s ruling is a major breakthrough as the judge recognised that Shell’s global headquarters in the Netherlands had a duty of care toward the Oruma villagers to prevent such a situation from happening. Eric de Brabandere, professor in International Dispute Settlement at Leiden University, said that “This case is of great importance because it is the first time a parent company is held responsible for what happens in a region in which it is not active itself,” However, Shell’s mother company only holds the liability to act on prevention and not for the damages done. Despite this relatively positive outcome, proceedings took more than a decade and was only made possible by strong NGO support of the victims.

The above mentioned cases expose the weakness of current international legal framework as well as the EU law in enabling an effective access to remedy and legal justice in cross-border situations.

If you encountered difficulties, how and in which context do you consider they could (should) be addressed?

An international binding legal framework and an efficient judicial cooperation is needed so that victims of such cases could effectively seek justice and the remedy for the harm done. Unfortunately, the current patchwork of not well-aligned national laws results in loopholes that resourceful corporations use. An EU framework for corporate due diligence with judicial enforcement with liability and compensation in case of harm would be a significant step forward.

Parent companies should stop hiding from responsibility by saying that they were not aware or did not control their local subsidiaries actions. As part of the European corporate due diligence rules, companies should be responsible for the actions of their subsidiaries within and outside Europe.
Section IV: Other elements of sustainable corporate governance

Question 20: Stakeholder engagement

Better involvement of stakeholders (such as for example employees, civil society organisations representing the interests of the environment, affected people or communities) in defining how stakeholder interests and sustainability are included into the corporate strategy and in the implementation of the company’s due diligence processes could contribute to boards and companies fulfilling these duties more effectively.

Question 20a: Do you believe that the EU should require directors to establish and apply mechanisms or, where they already exist for employees for example, use existing information and consultation channels for engaging with stakeholders in this area?

☒ I strongly agree
☐ I agree to some extent
☐ I disagree to some extent
☐ I strongly disagree
☐ I do not know
☐ I do not take position

Please explain.

The due diligence process should be used to identify risks in stakeholder engagement for certain groups, and identify additional measures required to mitigate these risks. Affected stakeholders should be engaged at all stages of the due diligence process. This concerns the identification and assessment of human rights and environmental risks, as well as determination of the appropriate actions and the monitoring and evaluation of their effectiveness.

Question 20b: If you agree, which stakeholders should be represented? Please explain.

Sustainability matters and stakeholders interests beyond those of shareholders are increasingly important for the success of the company.

We suggest that through a representation on boards of large companies, employees’ representatives should be involved in deciding on strategic matters. Employees have a strong interest in company’s long-term success and sustainable performance.

Affected and potentially affected stakeholders should be consulted in all stages of the due diligence process, from the identification of risks to the determination of appropriate actions, to monitoring and evaluating the effectiveness of the company’s actions to prevent, mitigate and remedy the impacts.

Question 20c: What are best practices for such mechanisms today? Which mechanisms should in your view be promoted at EU level? (tick the box, multiple choice)

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<th>Advisory body</th>
<th>Is best practice</th>
<th>Should be promoted at EU level</th>
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Targeted meetings with specific groups of stakeholders may be appropriate to ensure meaningful engagement with those who are differently or disproportionately affected, or who may face barriers to involvement in other processes. However, companies should have a flexibility on how they engage with stakeholders, as long as there is a due process in place, overseen by directors, and publicly reported on.

Following the lead of certain countries, e.g. France, employees should be represented on corporate boards of large companies, enjoy full board members’ rights, and therefore be involved in all strategic decisions. Employees have a strong interest in company’s long-term success and sustainable performance. As demonstrated especially in recent years, employees are keen to be involved and can have a positive effect on corporate decisions including on environmental issues, like addressing climate change: [https://www.geekwire.com/2019/7600-amazon-employees-demand-action-climate-change-advance-annual-meeting/](https://www.geekwire.com/2019/7600-amazon-employees-demand-action-climate-change-advance-annual-meeting/).

**Question 21:** Remuneration of directors

Current executive remuneration schemes, in particular share-based remuneration and variable performance criteria, promote focus on short-term financial value maximisation (Study on directors’ duties and sustainable corporate governance).

Please rank the following options in terms of their effectiveness to contribute to countering remuneration incentivising short-term focus in your view.

This question is being asked in addition to questions 40 and 41 of the Consultation on the Renewed Sustainable Finance Strategy the answers to which the Commission is currently analysing.

**Ranking 1-7 (1: least efficient, 7: most efficient)**

<table>
<thead>
<tr>
<th>Option</th>
<th>Rank</th>
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<tbody>
<tr>
<td>Restricting executive directors’ ability to sell the shares they receive as pay for a certain period (e.g. requiring shares to be held for a certain period after they were granted, after a share buy-back by the company)</td>
<td>6</td>
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<tr>
<td>Regulating the maximum percentage of share-based remuneration in the total remuneration of directors</td>
<td>7</td>
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<tr>
<td>Regulating or limiting possible types of variable remuneration of directors (e.g. only shares but not share options)</td>
<td>7</td>
</tr>
<tr>
<td>Making compulsory the inclusion of sustainability metrics linked, for example, to the company’s sustainability targets or performance in the variable remuneration</td>
<td>7</td>
</tr>
<tr>
<td>Mandatory proportion of variable remuneration linked to non-financial performance criteria</td>
<td>7</td>
</tr>
<tr>
<td>Requirement to include carbon emission reductions, where applicable, in the lists of sustainability factors affecting directors’ variable remuneration</td>
<td>7</td>
</tr>
<tr>
<td>Taking into account workforce remuneration and related policies when setting director remuneration</td>
<td>7</td>
</tr>
<tr>
<td>Other option, please specify</td>
<td></td>
</tr>
<tr>
<td>None of these options should be pursued, please explain</td>
<td></td>
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</table>
Please explain:

Directors’ remuneration (referring to both executive and non-executive directors) is a very important tool to incentivise behaviours and therefore strategically important decisions. Directors’ remuneration has an important impact on how corporate strategies are formulated and how companies are run. Linking directors’ remuneration with corporate sustainable performance and sustainability targets is a very effective and indispensable tool to put companies on a sustainable path.

Currently, directors’ variable remuneration is often linked with the share price. This can lead to an undue focus on share price fluctuations and short-termism. Directors’ remuneration is also frequently linked to the production outputs which, for some sectors, can have detrimental effects.

A recent study performed by Carbon Tracker shows that reforms to align oil and gas executive compensation with the realities of the energy transition are too slow. According to the study “90% of companies directly reward executives for production or reserves increases in some shape or form, a figure virtually unchanged since 2017. These targets encourage a focus on size over shareholder value, exacerbating stranding risks.”

Therefore, we strongly suggest to link 50% of directors’ variable remuneration to clearly defined and measurable sustainability-related objectives / targets which should be in sync with the sustainability targets reflected in the corporate strategy. A proportion of directors’ variable remuneration could be aligned with the financial performance of the company over a period - of several years. However, we suggest to limit strictly the alignment of directors’ remuneration with the share price: granting and offering of share options should be banned altogether whilst granting and offering of shares should be strictly limited in terms of size. If directors want to own shares beyond the limit imposed on the number of shares they could be granted, they should purchase them on their own account and on the same terms as investors.

Linking directors’ remuneration with the share price incentivises undue focus on this metric, which, in many cases, is not an adequate reflection of a company’s intrinsic value. Excessive attention to share price diverts directors’ attention from pursuing sustainable value creation, which can only be the result of a long term positive financial performance and a combined maximisation of positive impacts and minimization of negative impacts on the environment and society.

Question 22: Enhancing sustainability expertise in the board

Current level of expertise of boards of directors does not fully support a shift towards sustainability, so action to enhance directors’ competence in this area could be envisaged (Study on directors’ duties and sustainable corporate governance).

Please indicate which of these options are in your view effective to achieve this objective (tick the box, multiple choice).

☒ Requirement for companies to consider environmental, social and/or human rights expertise in the directors’ nomination and selection process

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☒ Requirement for companies to have a certain number/percentage of directors with relevant environmental, social and/or human rights expertise
☐ Requirement for companies to have at least one director with relevant environmental, social and/or human rights expertise
☒ Requirement for the board to regularly assess its level of expertise on environmental, social and/or human rights matters and take appropriate follow-up, including regular trainings
☐ Other option, please specify
☐ None of these are effective options

Please explain:

Given the growing strategic importance of sustainability risks on company operations and impacts that business operations have the environment and society, directors must ensure they have the necessary collective expertise on sustainability matters within the board. The appropriate number of board members with such expertise should be decided based on the company’s business model (e.g. sustainability risks and adverse impacts are more pertinent for an oil company than for an IT company) as well as physical, transition and disruption risks that the company faces.

Obviously, that also means that companies should be required to consider environmental, social and/or human rights expertise in the directors’ nomination and selection process and that corporate boards should regularly undergo an assessment of their level of expertise on environmental, social and/or human rights matters.

Traditionally boards are composed of ‘pure business’ people. In light of the growing strategic importance of sustainability matters, we suggest that directors be trained in sustainability matters, including sustainability risks and adverse impacts.

Question 23: Share buybacks

Corporate pay-outs to shareholders (in the form of both dividends and share buybacks) compared to the company’s net income have increased from 20 to 60 % in the last 30 years in listed companies as an indicator of corporate short-termism. This arguably reduces the company’s resources to make longer-term investments including into new technologies, resilience, sustainable business models and supply chains. (A share buyback means that the company buys back its own shares, either directly from the open market or by offering shareholders the option to sell their shares to the company at a fixed price, as a result of which the number of outstanding shares is reduced, making each share worth a greater percentage of the company, thereby increasing both the price of the shares and the earnings per share.) EU law regulates the use of share-buybacks [Regulation 596/2014 on market abuse and Directive 77/91, second company law Directive].

In your view, should the EU take further action in this area?

☐ I strongly agree
☒ I agree to some extent
☐ I disagree to some extent
☐ I strongly disagree
☐ I do not know
☐ I do not take position

Question 23a: If you agree, what measure could be taken?
An important increase of corporate pay-outs to shareholders coming at the expense of longer-term investments is indeed worth analysing. Share buy-backs indeed may be a reflection of short-termism in capital markets. However, it depends on the circumstances, maturity of the company, etc.

From a corporate finance standpoint, buying-back shares is similar to paying out a dividend. However, their respective tax treatment is usually different. An additional incentive and often essential reason for share buy-backs is to put upward pressure on the share price. As directors’ remuneration is frequently linked to the share price, this can incentivise directors to take decisions that increase the share price instead of promoting sustainable value creation.

Therefore, we suggest to remove the currently existing incentives for share buy-backs. That means: 1) encouraging an equal tax treatment of share buy-backs compared to dividends; and 2) limiting strictly the level of directors’ remuneration linked to the share price (see our response to question 21).

**Question 24:** Do you consider that any other measure should be taken at EU level to foster more sustainable corporate governance?  
If so, please specify:

We see value of giving equal opportunities to both genders. It will be essential, going forward, to ensure women empowerment in corporate decision-making bodies. The reason for this is simple to fathom: women should be given the same opportunities as men to access positions of powers, as well functioning institutions are institutions that manage to reflect as closely as possible the diversity of society.

Obviously, diversity is not only related to gender, but also to social the background (including education), age, ethnicity and, most importantly, to **diversity of professional competences and skills**.

In the context of the growing sustainability crisis, and as mentioned in response to Q 22, expertise on environmental, social and/or human rights matters must also be reflected on the two main decision-making bodies of corporations, i.e. corporate boards and executive committees.

Many responsible investors consider that an executive committee composition reflecting the diversity of the company itself is particularly important as it reflects the reality of the balance of power of the organisation. In essence, executive committee composition should reflect the gender balance (and, more generally, the diversity) encountered in the overall company.

We therefore suggest to consider **EU measures to address an improved diversity on corporate boards and within the corporate executive committee**. The objective should be to achieve gender balance on the board and gender representation reflecting the situation of the overall company on the executive committee (if a company’s employees are 65% women (men), then the executive committee should be composed of 65% of female (male) members).

**Section V: Impacts of possible measures**

**Question 25:** Impact of the spelling out of the content of directors’ duty of care and of the due diligence duty on the company

Please estimate the impacts of a possible spelling out of the content of directors’ duty of care as well as a due diligence duty compared to the current situation. In your understanding and own assessment, to what extent will the
impacts/effects increase on a scale from 0-10? In addition, please quantify/estimate in quantitative terms (ideally as percentage of annual revenues) the increase of costs and benefits, if possible, in particular if your company already complies with such possible requirements.

<table>
<thead>
<tr>
<th>Non-binding guidance. Rating 0-10</th>
<th>Introduction of these duties in binding law, cost and benefits linked to setting up/improving external impacts’ identification and mitigation processes Rating 0 (lowest impact)-10 (highest impact) and quantitative data</th>
<th>Introduction of these duties in binding law, annual cost linked to the fulfilment of possible requirements aligned with science-based targets (such as for example climate neutrality by 2050, net zero biodiversity loss, etc.) and possible reorganisation of supply chains Rating 0 (lowest impact)-10 (highest impact) and quantitative data</th>
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</thead>
<tbody>
<tr>
<td>Administrative costs including costs related to new staff required to deal with new obligations</td>
<td></td>
<td></td>
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<td>Litigation costs</td>
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<tr>
<td>Other costs including potential indirect costs linked to higher prices in the supply chain, costs liked to drawbacks as explained in question 3, other than administrative and litigation costs, etc. Please specify.</td>
<td>Better performance stemming from increased employee loyalty, better employee performance, resource efficiency</td>
<td>Competitiveness advantages stemming from new customers, customer loyalty, sustainable technologies or other opportunities</td>
</tr>
<tr>
<td>Better risk management and resilience</td>
<td></td>
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<td>Innovation and improved productivity</td>
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<td>Better environmental and social performance and more reliable reporting attracting investors</td>
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</table>
Other impact, please specify

**Question 26: Estimation of impacts on stakeholders and the environment**

A **clarified duty of care and the due diligence duty** would be expected to have **positive impacts on stakeholders and the environment**, including in the supply chain. According to your own understanding and assessment, if your company complies with such requirements or conducts due diligence already, please quantify / estimate in quantitative terms the positive or negative impact annually since the introduction of the policy, by using examples such as:

- **Improvements on health and safety of workers in the supply chain**, such as reduction of the number of accidents at work, other improvement on working conditions, better wages, eradicating child labour, etc.
- **Benefits for the environment through more efficient use of resources**, recycling of waste, reduction in greenhouse gas emissions, reduced pollution, reduction in the use of hazardous material, etc.
- **Improvements in the respect of human rights**, including those of local communities along the supply chain
- **Positive/negative impact on consumers**
- **Positive/negative impact on trade**
- **Positive/negative impact on the economy (EU/third country)**

We understand this question is targeted at companies. However, we believe it is also important to look at potential impacts of the envisaged measures on the environment and society including corporate workers, as well as the cost of inaction.

Also, when it comes to certain aspects like breach of human rights or environmental rules or norms, cost should not really matter. And if a business undertaking would entail breaching human rights or destroying environment to be financially profitable, it should not be pursued.

A **European framework on more specific duty of care**, requiring companies to fully integrate sustainability risks and adverse impacts’ in corporate strategy and a mandatory due diligence duty would positively contribute to:

- Respect of human and labour rights not only within the EU but, depending on how the rules would eventually be formulated, also in developing countries. This includes reduction in human trafficking, child labour and modern-day slavery.
- **Improved safety and working conditions of workforce throughout the global supply chains**.
- **Improved health and standard of life of people around the world** given the globalised supply chains.
- **Improved environmental impact of corporate operations** through consideration of sustainability impacts and better compliance with environmental norms, reduced use of toxic chemicals, safer and more environmentally friendly production methods, etc.
- **Mitigation of climate change**.
- **Better consideration of rights and interest of indigenous people and decline in land grabs**.

- Etc.