The EU Sustainable Governance Consultation and the Missing Link to Soft Law

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Guido Ferrarini
University of Genoa, ECLE Group, EUSFiL and ECGI

Michele Siri
University of Genoa, EUSFiL

Shanshan Zhu
University of Genoa, EUSFiL

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Keywords: sustainable corporate governance, soft law, corporate governance codes, short-termism, directors' duties, sustainable finance, corporate governance, corporate social responsibility, shareholder primacy, shareholder value, shared value, social value, stakeholder theory, stakeholder governance, stakeholder capitalism, sustainability

JEL Classifications: G30, G32, G38, K20, K32, L21, M14, P12

Guido Ferrarini*
Emeritus Professor of Business Law
University of Genoa, Department of Law
Via Balbi, 22,
16126 Genoa, Italy
e-mail: guido.ferrarini@unige.it

Michele Siri
Professor of Business Law, Jean Monnet Chair on European Union
Financial and Insurance Markets Regulation
University of Genoa, Department of Law
Via Balbi, 22,
16126 Genoa, Italy
e-mail: michele.siri@unige.it

Shanshan Zhu
Post-doctoral Research Fellow, EUSFiL Academic Fellow
University of Genoa, Department of Law
Via Balbi, 22,
16126 Genoa, Italy
e-mail: shanshan.zhu@giuri.unige.it

*Corresponding Author

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Guido Ferrarini

guido.ferrarini@unige.it

Emeritus Professor of Business Law, University of Genoa;
Academic Member and Steering Committee Member, EUSFiL;
Fellow and Research Member, ECGI;
Member ECLE Group

Michele Siri

michele.siri@unige.it

Full Professor of Business Law, University of Genoa
Jean Monnet Chair on European Union Financial and Insurance Markets Regulation
EUSFiL Director

Shanshan Zhu

shanshan.zhu@giuri.unige.it

Post-doctoral Research Fellow, University of Genoa
EUSFiL Academic Fellow

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I. INTRODUCTION

1. Purpose and scope of the paper

In this paper, we examine whether reform of EU company law is needed to make corporate governance more sustainable. We focus on the European Commission's consultation on this topic and try to answer some of the key questions in the consultation questionnaire.[1] At the same time, we consider a few additional issues, which have not been properly touched upon by the Commission in its questionnaire, concerning the role of corporate governance codes and other types of soft law, mainly of international origin, in promoting sustainable governance. As we argue throughout our paper, most of the consultation questions already find an answer either in corporate governance codes or in the other soft law instruments of international origin. Omitting to consider the important practical role of these documents might seriously impair the consultation's outcomes and negatively impact the legislation that the Commission may propose as a result. Moreover, we argue that also the broader context of EU company law reform should be considered. Several measures have been adopted in recent years, which were similarly motivated by the intention to curb corporate short-termism and promote sustainability in firms' management. We conclude that failure to consider soft law instruments and the broader picture of EU company law concerning managerial incentives and shareholder engagement could seriously impair pending reform efforts concerning directors' duties and their link to sustainability.

In the present Section of this paper, we introduce the Commission's initiative on sustainable governance and briefly consider the main scholarly criticisms. In Section II, we examine how corporate governance codes have been recently adapted to sustainability requirements and summarize the outcomes of recent research conducted by two of us in this respect.[2] In Section III, we try to answer some of the Commission's core questions in its questionnaire and comment on how corporate governance codes and other instruments of soft law already respond to these questions. In Section IV, we put the same issues in a broader context and show how recent EU company law reforms have already tried to solve some of the problems that the Commission is now considering. In section V we conclude.

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[1] See the European Commission Consultation, available at https://ec.europa.eu/info/law/better-regulation/have-your-say/initiatives/12548-Sustainable-corporate-governance. See also EU Commission, Inception impact assessment, Ares(2020)4034032.

[2] See Michele Siri & Shanshan Zhu, 'Integrating sustainability in EU Corporate Governance Codes', in Danny Busch, Guido Ferrarini and Seraina Grünewald (eds.) *Sustainable Finance in Europe* (London: Palgrave MacMillan, Forthcoming).

2. The Commission's sustainable governance initiative

The Commission has recently increased its efforts to support the transition to a sustainable EU economy, in line with its commitment to achieving the objectives of the 2015 Paris Agreement[3] and the UN Sustainable Development Goals.[4] To this purpose, the EU legislator initiated a reform program in 2018 with the formal adoption of the Action Plan "Financing Sustainable Growth" ('Action Plan'),[5] which aims to enhance the connection between the financial industry and sustainable development.

The Action Plan consists of ten key actions,[6] the last of which concerns the promotion of sustainable corporate governance and the reduction of short-termism in capital markets. According to the Commission, a similar choice is justified by the significant contribution that corporate governance can give to promote "...a more sustainable economy, allowing companies to take the strategic steps necessary to develop new technologies, to strengthen business models and to improve performance", but also to "improve their risk management practices and competitiveness".[7] In line with this approach and in consideration of the complexity of the issues at stake, the EU Commission committed itself to carry out analytical and consultative work with relevant stakeholders to assess: (i) the possible need to require corporate boards to develop and disclose a sustainability strategy, including appropriate due diligence throughout the supply chain, and measurable sustainability targets; and (ii) the possible need to clarify the rules according to which directors are expected to act in the company's long-term interest.

(i) As to the first topic, the Commission published in February 2020 the 'Study on due diligence requirements through the supply chain',[8] prepared on its behalf by the British Institute

[3] UN, Paris Agreement on Climate Change, UN Doc. FCCC/CP/2015/L.9/Rev.1 (12 December 2015).

[4] EU Commission, Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions, Next steps for a sustainable European future European action for sustainability, COM(2016) 739 final.

[5] EU Commission. Communication from the Commission to the European Parliament, the European Council, the Council, the European Central Bank, the European Economic and Social Committee and the Committee of the Regions, Action Plan: Financing Sustainable Growth, COM (2018) 97 final (March 2018).

[6] The 10 key actions are: a) establishing an EU classification system for sustainable activities; (b) creating standards and labels for green financial products; (c) fostering investment in sustainable projects; (d) incorporating sustainability when providing financial advice; (e) developing sustainability benchmarks; (f) better integrating sustainability in ratings and market research; (g) clarifying institutional investors' and asset managers' duties; (h) incorporating sustainability in prudential requirements; (i) strengthening sustainability disclosure and accounting rule-making; and (l) fostering sustainable corporate governance and attenuating short-termism in capital markets. See also Michele Siri & Shanshan Zhu, 'Will the EU Commission Successfully Integrate Sustainability Risks and Factors in the Investor Protection Regime? A Research Agenda' (2019) *Sustainability*, 11, 1-23.

[7] See EU Commission, n 5.

[8] Lise Smit, Claire Bright, Robert McCorquodale, Matthias Bauer, Hanna Deringer, Daniela Baeza- Breinbauer, Francisca Torres-Cortés, Frank Alleweldt, Senda Kara and Camille Salinier and Héctor Tejero Tobed, 'Study on due diligence requirements through the supply chain, Final report' (January 2020), available at https://op.europa.eu/en/publication-detail/-/publication/8ba0a8fd-4c83-11ea-b8b7-01aa75ed71a1/language-en.

of International and Comparative Law (BIICL) in partnership with Civic Consulting and LSE Consulting. The Study was built on an extensive research and assessment process including surveys, interviews, case studies, desktop and legal research, and involving 334 individuals among SMEs and large companies, business and industry associations, civil society, trade unions and practising lawyers. It found that about one-third of business respondents undertake due diligence, which takes into account all human and environmental impact, while a further third undertake due diligence only in certain areas. According to the BIICL Study, the most significant incentives for this type of behaviour derive from reputational risks, investor pressure and consumer pressure. Moreover, the Study found that the standard of due diligence set out in the UN Guiding Principles on Business and Human Rights is being adopted as a standard framework. Interestingly, the Study also found that the most frequently adopted due diligence tools include contractual clauses in the context of supplier contracts, codes of conduct and audits, while divestment is the least used tool.

The Study considered four regulatory options at EU level concerning due diligence requirements: 1) no policy change; 2) new voluntary guidelines; 3) new regulation requiring due diligence reporting; and 4) new regulation requiring mandatory due diligence as a legal duty of care. Among the proposed options, No. 4) represented the most favoured, as the majority of respondents agreed that a similar solution would be the most beneficial to business in terms of ensuring legal certainty, harmonization across the EU and creation of a level playing field. Overall, while most respondents were in favour of a policy change for the introduction of a general standard at EU level, respondents for industry organizations - with the exception of multinational companies - expressed a contrary opinion, especially in relation to the introduction of mandatory due diligence. Moreover, different views were expressed in relation to liability regimes and the enforcement models to establish. However, on 11 March 2021 the European Parliament adopted, with a large majority, a legislative report by its Legal Affairs Committee on corporate due diligence and corporate accountability, providing recommendations to the European Commission on the next steps to take.[9] In particular, a directive on corporate due diligence and accountability would require Member States to lay down rules to establish and effectively implement a due diligence strategy, involving relevant stakeholders during the process.

(ii) As to the second topic, in July 2020 the "Study on directors' duties and sustainable corporate governance", prepared by EY, was published by the Commission's DG Justice and

[9] See European Parliament, Resolution of 10 March 2021 with recommendations to the Commission on corporate due diligence and corporate accountability (2020/2129(INL))

Consumers.[10] The Study aimed in particular to "assess the root causes of 'short termism' in corporate governance, discussing their relationship with current market practices and/or regulatory frameworks" and to "identify possible EU-level solutions, also with a view to contributing to the attainment of the UN Sustainable Development Goals and the goals of the Paris Agreement on climate change."[11] To this end, two main tasks were performed: 1) the analysis of the state of play and potential problems, and 2) the identification of possible options and their potential impact. As to the first, the Study - based on literature review, legal review, interviews and surveys - identified as a core problem the "trend for publicly listed companies within the EU to focus on short-term benefits of shareholders rather than on the long-term interests of the company". It also found the problem's root causes lie in the regulatory framework and market practices. Specifically, the collected data indicate an upward trend in shareholder pay-outs, which increased from 20% to 60% of net income during the period considered in the Study, while the ratio of investment (capital expenditure) and R&D spending to net income declined by 45% and 38%, respectively.

The Study then identified seven key problem drivers: (1) directors' duties, and company's interest to favour the short-term maximization of shareholder value; (2) growing pressures from investors with a short-term horizon; (3) companies lack a strategic perspective over sustainability; (4) board remuneration structures that incentivize the focus on short-term shareholder value; (5) current board composition inadequacy to support a shift towards sustainability; (6) insufficient stakeholder engagement and involvement in current corporate governance frameworks and practices; and (7) limited enforcement of the directors' duty to act in the long-term interest of the company.[12] In light of the identified problems, the Study called for EU intervention to tackle short-termism and ensure a level playing field for European companies in pursuing three specific objectives: 1) strengthening the role of directors in pursuing their company's long-term interest, 2) improving directors' accountability towards integrating sustainability into corporate decision-making and, 3) promoting corporate governance practices that contribute to company sustainability. The Study also analysed the impacts of possible EU level options/approaches addressing each of the seven identified drivers, including both non-legislative/soft measures (such as the publication of communications, guidance documents, green papers or recommendations)

[10] EY, Study on directors' duties and sustainable corporate governance, July 2020, available at https://op.europa.eu/en/publication-detail/-/publication/e47928a2-d20b-11ea-adf7-01aa75ed71a1/language-en/format-PDF.

[11] Ibidem, i.

[12] Ibidem, vi.

and legislative/hard solutions (such as the adoption or amendment of directives and recommendations).

Based on the findings of the BIICL and the EY Studies, in October 2020 the Commission launched the Sustainable Corporate Governance Initiative,[13] seeking feedback from stakeholders on the need for EU intervention on sustainable corporate governance and on the scope and structure of any such intervention, in view of enabling companies to focus on long-term sustainable value creation rather than short-term benefits. The relevant Consultation Document includes 26 questions, which fall under 4 sections: I. Need and objectives for EU intervention on sustainable corporate governance; II. Directors' duty of care - stakeholders' interests; III. Due diligence duty; IV. Other elements of sustainable corporate governance. In this paper, we shall focus on the first two sections, which are mainly based on the EY Study.

3. **Main criticism of the Commission's initiative**

M. Roe, H. Spamann, J. Fried and C. Wang offer a devastating critique of the EY Report.[14] First of all, they lament that "the Report conflates time-horizon problems (short-termism) - which are the focus of its evidence collection - with externalities and distributional concerns".[15] We share their criticism and highlight that the externalities at issue are particularly those that negatively affect the environment and society as a result of corporate actions. The authors essentially argue that tackling short-termism is the wrong way to proceed. A long-term perspective in the management of a company does not guarantee that the latter's negative externalities will be reduced. The same externalities can reverberate on the company at issue, which might be damaged by environmental and social failures either directly or indirectly through a loss of reputation. The incentives for the company to reduce them in advance are greater here than when they mainly affect third parties. The Commission would want companies to internalize the negative externalities they produce by clarifying directors' duties. However, as we argue in this paper, such a reform is not necessary as other instruments are available, including soft law, non-financial disclosure and managerial incentives, to reach similar or better results. Also, controlling shareholders and institutional investors can work in the same direction and should be considered in the policy discussion on

13 European Commission, n 1.

14 Mark J. Roe, Holger Spamann, Jesse M. Fried, and Charles C.Y. Wang, 'The European Commission's Sustainable Corporate Governance Report: A Critique' (2020) European Corporate Governance Institute - Law Working Paper 553/2020.

15 Ibidem.

sustainable governance.[16] With increasing frequency, they exert pressure on companies and their leaders, engaging them in the pursuit of sustainable growth.

Roe et al. also argue that the EY Report's main ostensible evidence for an increase in short-termism is "rising *gross* pay-outs to shareholders (dividends and repurchases) coupled with declining investment (...) at certain large listed companies". However, the more relevant measure to assess corporations' ability to fund long-term investments is *net* pay-outs, which "have risen but only by recovering from earlier unsustainably low levels, while still leaving plenty of funds available for investment". They also criticise the Report for failing "to use a full sample of EU listed companies, an analysis of which shows that CAPEX and R&D actually increased over the period indicated in the Report".[17] A similar critique has been advanced by the ECLE group, noting that "the chosen denominator does not include capital inflows through equity issuances and investments in the business" and suggesting that "the observed modest increase in the pay-out ratio after the financial crisis could be due to the exceptionally favourable conditions in the credit markets, so that the increase in dividends and buybacks represents a replacement of equity by debt, not a sign of short-termism.[18] Other commentators have similarly suggested that the extremely low interest rates that most countries have experienced in recent years have pushed companies either to pay dividends to shareholders or to buy back their shares rather than holding cash on their accounts.[19] Also, the inclusion of UK companies in the sample used by EY might have biased the conclusions, which were intended to be the basis for reforms addressing only the EU27.[20]

Roe et al. also disapprove of the Report's individual proposals for EU policy measures, arguing that they stand on shaky foundations because their ostensible target (short-termism) may be modest, while the real problems (externalities and distribution) have not been articulated in the Report.[21] We consider this criticism further below when examining the Commission's questionnaire, which has taken some of the Study's proposals into account.

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16 Alessio M. Pacces, 'Sustainable Corporate Governance: The Role of the Law' (2020), European Corporate Governance Institute - Law Working Paper No. 550/2020, Amsterdam Law School Research Paper No. 2020-66, Amsterdam Center for Law & Economics Working Paper No. 2020-05.

17 Roe et al., n 13. See also Wolf-Georg Ringe, Alexander Bassen, and Kirsten Lopatta, 'EC Corporate Governance Initiative Series: 'The EU Sustainable Corporate Governance Initiative—room for improvement', Opinion (2020), Oxford Business Law Blog, available at https://www.law.ox.ac.uk/business-law-blog/blog/2020/10/ec-corporate-governance-initiative-series-eu-sustainable-corporate.

18 European Company Law Expert Group (ECLE), 'Comment regarding the EY Study on directors' duties and sustainable corporate governance' (2020), available at https://europeancompanylawexperts.wordpress.com/publications/european-commission-study-on-directors-duties-and-sustainable-corporate-governance. See also Karel Lannoo, Jesper Lau Hansen and Apostolos Thomadakis, 'Are European Listed corporations sort-termist?' (2021), *ECMI Commentary,* 71.

19 Assia Elgouacem and Riccardo Zago, 'Share Buybacks, Monetary Policy and the Cost of Debt" (2020), Working Paper, No. 773, Banque de France.

20 See also Karel Lannoo et al., n 18.

21 Roe et al., n 13; Ringe et al, n 17.

II. ROLE OF CORPORATE GOVERNANCE CODES AND OTHER SOFT LAW INSTRUMENTS

4. The missing link to corporate governance codes

Based on the EY Report's impact assessment – which generally considered soft law approaches (option A and B of each driver) as only moderately effective - the Commission has not considered the role of soft law as a tool for specifying the directors' duty of care. However, the national codes of corporate governance and the other soft law instruments that we mention below may successfully contribute to this objective in at least two ways. Some codes already specify the duty of care along the lines suggested by the Commission in its questionnaire. Following their example, the Commission could simply issue a recommendation to the Member States that the latter would follow through an amendment (if needed) of their national codes of corporate governance.[22] If EU legislation were nonetheless adopted to clarify the directors' duties as to sustainability, the corporate governance codes could work as a complement to legislation and further specify the standards established at EU level (for instance, in relation to directors' skills and competencies in the area of sustainability).

In order to analyse the potential contribution of corporate governance codes to sustainability, we briefly examine the state of the art in this area. While several studies have investigated the effectiveness of corporate governance codes in the EU,[23] only a few have considered the role of

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[22] See, for instance, European Commission. Internal Market and Services. Report of the Reflection Group on the Future of EU Company Law (2011); European Commission. Green Paper on the EU Corporate Governance Framework; COM (2011)164 Final.; Commission Recommendation 2005/162/EC of 15 February 2005 on the role of non-executive or supervisory directors of listed companies and on the committees of the (supervisory) board; Commission Recommendation 2004/913/EC of 14 December 2004 on fostering an appropriate regime for the remuneration of directors of listed companies.

[23] See, for example: Eddy Wymeersch, 'European corporate governance codes and their effectiveness', in M. Belcredi & G. Ferrarini (Eds.) *Boards and shareholders in European listed companies: facts, context and post-crisis reforms* (Cambridge: Cambridge University Press, 2013), 67–142; Peter Böckli, Paul L. Davies, Eilis Ferran, Guido Ferrarini, José M. Garrido Garcia, Klaus J. Hopt, Alain Pietrancosta, Katharina Pistor, Markus Roth, Rolf Skog, Stanislaw Soltysinski, Jaap Winter, Eddy Wymeersch, 'Making Corporate Governance Codes More Effective: A Response to the European Commission's Action Plan of December 2012', Oxford Legal Studies Research Paper No. 56/2014; Idoya Ferrero-Ferrero and Robert Ackrill, 'Europeanization and the Soft Law Process of EU Corporate Governance: How Has the 2003 Action Plan Impacted on National Corporate Governance Codes?' (2016), *Journal of Common Market Studies*, 54(4), 878-895; Markus Stiglbauer and Patrick Velte, 'Impact of Soft Law Regulation by Corporate Governance Codes on Firm Valuation. The Case of Germany' (2014), *International Journal of Business in Society*, 14, 395-406; Marcello Bianchi, Angelo Ciavarella, Valerio Novembre, and Rossella Signoretti, 'Comply or Explain: Investor Protection Through the Italian Corporate Governance Code' (2011), *Journal of Applied Corporate Finance*, 23(1), 107-121; and RiskMetrics Group

the codes in promoting environmental and social responsibility.[24] Two of us recently investigated the level of integration of sustainability in corporate governance codes across the EU Member States.[25] Our study evaluated, in particular, the topic of sustainability integration according to the following indicators:

(a) reference to sustainable development/CSR/environmental and social responsibility in the definition of corporate governance (when provided);

(b) inclusion of sustainability concerns in the description of the function and purpose of the code;

(c) specific provisions/recommendations addressing CSR/sustainability concerns;

(d) definitions of stakeholders and their rights;

(e) provisions concerning employees' rights and engagement;

(f) gender diversity criteria for board composition;

(g) recommended attribution of CSR functions to a pre-existing board committee or to an *ad hoc* social responsibility committee;

(h) reference to non-financial criteria or to sustainable value creation in the design of compensation policy;

(i) reference to non-financial reporting requirements.

We found that the majority of European codes presently include sustainability considerations in their principles and recommendations.[26] In fact, 15 out of 27 corporate governance codes[27] either address CSR and sustainable value creation or devote an entire chapter/principle of the code to the duties of the company towards its stakeholders. For instance, the Italian and Spanish codes – following the model of the recently revised UK Code – recommend that the board of directors should lead the company towards 'sustainable success', which is defined by the Italian code as "the objective that guides the actions of the board of directors and that consists of creating long-term value for the benefit of the shareholders, taking into account the interests of other stakeholders relevant to the company".[28] Similar criteria should also guide the definition of the compensation

et al., 'Study on Monitoring and Enforcement Practices in Corporate Governance in the Member States' (2009), Study commissioned by the European Commission.

24 See Siri & Zhu, n 2; ; Beate Sjåfjell, 'When the Solution Becomes the Problem: The Triple Failure of Corporate Governance Codes', in J. J. Du Plessis and C.K. Low (eds), *Corporate Governance Codes for the 21st Century: International Perspectives and Critic* (Berlin: Springer, 2016), 23-55; and Daniel G. Szabó & Karsten E. Sørensen, 'Integrating Corporate Social Responsibility in Corporate Governance Codes in the EU' (2013), *European Business Law Review*, 24 (6), 781–828; Georgina Tsagas, 'A Proposal for Reform of EU Member States' Corporate Governance Codes in Support of Sustainability' (2020), *Sustainability*, 12(10), 4328.

25 See Siri & Zhu, n 2.

26 See also Sjåfjell, n 24; and Szabó & Sørensen, n 24.

27 Codes from Austria, Belgium, Bulgaria, Czech Republic, Croatia, Germany, Italy, Lithuania, Luxembourg, Malta, The Netherlands, Slovakia, Slovenia, Spain, and Sweden.

28 Italian Corporate Governance Code (2020), Principle I.

policy[29] and the activities performed within the internal control system.[30] Similarly, the codes from Austria, Belgium, Czech Republic, France, Germany, Netherlands and Sweden recommend that companies should be directed to ensure sustainable development/value creation/sustainable long-term value, to be understood as the maximization of shareholders' wealth with the permanent consideration of stakeholders' interests.[31] Other codes (from Bulgaria, Denmark, Luxembourg, Malta, Slovenia and Spain) include recommendations related to the adoption of CSR initiatives. According to our study, amongst the codes analysed, the most 'sustainability inclusive' is the Luxembourgish Code, which refers to a long-term and sustainable approach to value creation as one of the main drivers for the latest revision of the code. The Dutch and the Spanish codes are also good models in this respect.

Nonetheless, the numerous weaknesses and inconsistencies of existing codes suggest that further efforts are needed for the full integration of environmental and social issues in similar documents. A first shortcoming endangering the effectiveness of the codes regards their implementation,[32] which also depends on the enforcement of rules concerning the disclosure of compliance with the codes and the supervision by securities markets authorities.[33] Indeed, the lack of homogeneity amongst national codes, their custodians' different nature, and the monitoring of their implementation determine major differences in corporate governance practices. As argued by Wymeersch, all corporate governance codes issued in the EU follow a comply or explain approach, but the application of this principle is in practice quite diverse in the various jurisdictions.[34] Where a code has been adopted on a voluntary basis, corporate failure to fully or

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29 Ibidem, Principle XV.

30 Ibidem, Principle XIII.

31 Austrian Code of Corporate Governance (2020), Preamble; The 2020 Belgian Code On Corporate Governance (2020), §2.1, 2.2; German Corporate Governance Code (2020), p. 2; The Dutch Corporate Governance Code (2016), §1.1.1; and The Swedish Corporate Governance Code (2020), Principle 3.

32 The implementation and enforcement of corporate governance codes in the EU has been widely analyzed in the literature. See, for example, Erik Berglöf and Stijn Claessens, 'Enforcement and Corporate Governance' (2004), Policy Research Working Paper No.3409, World Bank; and Wymeersch, n 23; RiskMetrics Group et al., n 23.

33 The codes' effectiveness is addressed by the laws implementing Directive 2006/46/EC, which requires listed companies to include a corporate governance statement in their annual reports, together with a reference to the corporate governance code applied and the reasons for not applying individual provisions of it. The initial inadequacy of corporate governance reporting in relation to the comply or explain provision was remedied to some extent by the Commission, as announced in its 2012 Corporate Governance Action Plan, with the Recommendation on the quality of corporate governance reporting issued in 2014. However, an explicit link between corporate governance and sustainable development was missing until 2018 when the Commission Action Plan on financing sustainable growth was adopted. See Böckli, n 23; Wymeersch, n 23. See also Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions, Action Plan: European company law and corporate governance - a modern legal framework for more engaged shareholders and sustainable companies, COM(2012) 740 final.

34 Some codes have a mere self-regulatory nature, having been developed as recommendations by professional associations or academics who act as private custodians (e.g. Austria, France, Sweden and Portugal), while others have been issued in strict connection with stock exchanges, are referred to in the listing rules or separate recommendations, and are subject to the surveillance of stock exchanges (e.g. Luxembourg, Lithuania and Poland). Other codes are based

partially comply with it generally carries reputational consequences but no legal sanctions. The situation changes in jurisdictions where the corporate governance code is integrated into company law, and enforcement mechanisms are found in legal instruments. Nonetheless, given the diversity of the legal frameworks in which the individual codes have been developed, the enforcement instruments also vary.[35] Other weaknesses concern the monitoring of implementation practices, which in some countries are subject to yearly reports,[36] but not in others (namely the Czech Republic, Greece and Poland).[37] Moreover, it is difficult for both national "reporters" and scholars to assess the level of integration of sustainability concerns in corporate governance, given that provisions addressing them have only recently been adopted. As a result, only a few reports already consider the progress made by listed companies in performing sustainable governance practices.[38]

From a broader perspective, our findings[39] suggest that even influential documents such as the OECD Principles[40] and the UK Code[41] are not significantly advanced and inclusive as to sustainability, despite recent attempts to improve them in this respect. For instance, neither the OECD Principles nor the UK Code suggests establishing a sustainability committee. Moreover, the UK Code fails to provide a definition of stakeholders and does not recommend the adoption of a code of ethics, while the OECD Principles do not recommend that compensation should be linked to sustainability criteria. However, the OECD Principles make a clear reference to other more detailed soft law tools that provide guidelines as to business conduct, such as the OECD Guidelines for Multinational Enterprises, the Convention on Combating Bribery of Foreign Public

on the law and subject to public/mixed surveillance (e.g. the Netherlands and Germany). See OECD, 'The Corporate Governance Factbook' (2019), 41-47; and Eddy O. Wymeersch, 'Enforcement of Corporate Governance Codes' (2005), ECGI - Law Working Paper No. 46/2005.

35 Wymeersch, n 34, 4.

36 These are generally issued by national securities regulators (e.g. the Comisión Nacional del Mercado de Valores in Spain) in conjunction with or alternatively to stock exchanges (e.g. the Bourse de Luxembourg), private institutions (e.g. the Berlin Center of Corporate Governance in Germany) or and mixed private-public institutions (e.g. the Monitoring Committee in the Netherlands).

37 See OECD, 'The Corporate Governance Factbook' (2019), 47-49.

38 This is the case for Italy and Luxembourg. In Italy, Consob, Assonime and the Corporate Governance Committee already started monitoring sustainability integration into corporate governance practices in their last reports. A specific focus has been made on the link variable compensation and ESG objectives, an approach followed by about 33% of listed companies in 2020 (against 12% in 2019). The establishment of a sustainability committee was subject to analysis by Consob, which found that in 2018 a percentage of about 23% of listed companies established such committees, as suggested by the code. See Consob, 'Report on corporate governance of Italian listed companies' (2019); Assonime, 'La Corporate Governance in Italia: autodisciplina, remunerazioni e comply-or-explain' (2020); Corporate Governance Committee, 'Relazione 2020 sull'evoluzione della corporate governance delle società quotate' (2020). In Luxembourg, the 2018 report issued by the Bourse of Luxembourg found that, among the 13 companies listed on the national exchange, 85% published a sustainability report, but only 38% mentioned the adoption of a CSR strategy, and 62% established a sustainability committee. The reception of sustainability recommendations seems therefore positive, though a more robust and widespread evaluation of practices is still needed. See Bourse de Luxembourg, 'Rapport 2018: Application des X Principes de gouvernance d'entreprise' (2019).

39 See Siri & Zhu, note 2.

40 G20/OECD Code of Corporate Governance (2015).

41 UK Code (2018).

Officials in International Business Transactions, the UN Guiding Principles on Business and Human Rights, and the ILO Declaration on Fundamental Principles and Rights at Work.[42] A similar approach was followed by the drafters of the Slovak code, that considers "...as good practice for a company to commit itself to additional international principles, such as the UN Guiding Principles on Business and Human Rights or the OECD Guidelines for Multinational Enterprises".[43]

5. The role of international company law

The growing importance and diffusion of the principles and guidelines issued by international organizations and standard setters (including the IMF, the OECD, the World Bank, and the United Nations) have led some authors to identify a new field of the law which Mariana Pargendler significantly dubbed as "international corporate law" (ICL).[44] The emergence of ICL, according to her, has partially responded to the "interjurisdictional externalities and nationalist bias of domestic regimes" and, with specific reference to corporate responsibility towards the environment and society, it has the potential to fill the gaps in national legislations, by establishing new standards for corporate behaviour that take into account the negative effects of company activities on third parties. A significant role in this regard has been played by the UN and the OECD with the issuance of many guidelines and principles in the last decade.

As to the former, the two main guidelines addressing corporate responsibility are the UN Guiding Principles on Business and Human Rights [UN Guiding Principles] and the UN Global Compact Principles. The UN Guiding Principles provide standards for both States and business enterprises to prevent, address and remedy human rights abuses committed in business operations. On the corporate side, the guidance includes 14 principles specifically addressing the responsibilities of business enterprises in relation to the respect of human rights, providing also a set of operational recommendations going from the issuance of a specific policy on human rights to the performance of a human rights due diligence and the provision of remedies to the adverse impacts the company has caused or has contributed to generate with its actions. The Human Rights Council formally endorsed the Principles in 2011 and to date at least 377 large companies adopted a formal statement explicitly referring to human rights in compliance with Principle 16 of the UN

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42 OECD Code (2015), 10.

43 Corporate Governance Code for Slovakia (2016), 17.

44 Mariana Pargendler, 'The Rise of International Corporate Law' (2020), European Corporate Governance Institute - Law Working Paper, 555/2020, FGV Direito SP Research Paper Series n. Forthcoming.

Guiding Principles on Business and Human Rights.[45] Unlike the UN Guiding principles, the UN Global Compact is an initiative that global corporations can commit by respecting 10 key principles of business behaviour in human rights, labour, the environment, and corruption.[46] Currently, the UN Global Compact counts more than 12000 signatories in over 160 countries covering all business sectors.[47]

The OECD Guidelines for Multinational Enterprises, first adopted in 1976, are also important. They consist of a set of voluntary standards and principles for responsible business conduct addressed to multinational enterprises operating in or from the adhering countries. Specifically, the latest version of the OECD Guidelines was adopted in 2011 by the 42 OECD and non-OECD governments adhering to the OECD Declaration on International Investment and Multinational Enterprises, and today 49 governments have established a National Contact Point with the duty of ensuring the effectiveness of the OECD Guidelines by undertaking promotional activities, handling enquiries, and providing a grievance mechanism to resolve cases with regard to the non-observance of the recommendations. The OECD Guidelines cover a diverse range of topics related to business behaviour, from company disclosure and reporting on financial, social and environmental material information to the respect of employees, human rights, the environment, consumers interest and the fight against bribery and other illicit conducts, as well as the promotion of science and technology development, fair competition and tax compliance. To complement the standards of behaviour established by the OECD Guidelines, in 2018, the OECD Due Diligence Guidance for Responsible Business Conduct was adopted,[48] with the aim of providing practical support to business enterprises on the implementation of the OECD Guidelines. Moreover, the OECD has developed sector-specific due diligence guidance and good practice documents for the minerals,[49] agriculture[50] and garment and footwear supply chains,[51] as well as for the extractive sector.[52]

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[45] See https://old.business-humanrights.org/en/company-policy-statements-on-human-rights.
[46] See https://www.unglobalcompact.org/what-is-gc/mission/principles.
[47] See https://www.unglobalcompact.org/what-is-gc/participants.
[48] OECD (2018), OECD Due Diligence Guidance for Responsible Business Conduct.
[49] OECD (2016), OECD Due Diligence Guidance for Responsible Supply Chains of Minerals from Conflict-Affected and High-Risk Areas: Third Edition, OECD Publishing, Paris. http://dx.doi.org/10.1787/9789264252479-en.
[50] OECD, Recommendation of the Council on the OECD-FAO Guidance for Responsible Agricultural Supply Chains, OECD/LEGAL/0428.
[51] OECD (2017), OECD Due Diligence Guidance for Responsible Supply Chains in the Garment and Footwear Sector.
[52] OECD (2016), Recommendation of the Council on the Due Diligence Guidance for Meaningful Stakeholder Engagement in the Extractive Sector.

Notwithstanding the non-binding nature of such recommendations and their limited enforcement,[53] companies' policies and practices increasingly comply with these principles and standards and respond to investors' growing attention towards the ESG performance of investee companies, including the formal adoption of due diligence, environmental and human rights policies in line with international standards. In the sustainable investment strategies usually followed by institutional investors, the "norm-based screening" - which screens issuers against minimum standards of business practice based on international frameworks, such as the UN treaties, the UN Global Compact, the OECD Guidelines for Multinational Enterprises and the International Labour Organization standards - is one of the most commonly used for portfolio selection.[54] Moreover, common voluntary standards have been developed targeting investor stewardship obligations (such as the ICGN Global Stewardship principles and the EFAMA Stewardship Code)[55] or sustainable investment (such as the Principles for Responsible Investing),[56] which put further pressure on investors with regard to the sustainability-related initiatives and policies of investee companies.

A legal requirement for corporate due diligence, such as the one suggested in Section III of the Commission's questionnaire, could strengthen a practice already widespread in the market, especially if proposed Options 2 (carrying a minimum process and definition approach) or 3 (including further specific requirements) were adopted.[57] Due diligence requirements are beyond the present paper's scope, but their introduction in EU legislation would be in line with the Regulation (EU) 2020/852 on the establishment of a framework to facilitate sustainable investment [Taxonomy Regulation].[58] Article 3 of this Regulation requires business activities to comply with the minimum safeguards set out in Article 18 in order to be considered as "environmentally sustainable", i.e. to establish procedures "to ensure the alignment with the OECD Guidelines for Multinational Enterprises and the UN Guiding Principles on Business and

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53 See Pargendler, n 44.

54 See https://www.unpri.org/an-introduction-to-responsible-investment/an-introduction-to-responsible-investment-screening/5834.article. See also Eurosif, '2018 SRI Study for an overview of trends related to SRI strategies in Europe' (2018). See also ISS ESG, 'Norm-based Research Evaluation of ESG Controversies. Research Methodology' (2020), for an overview on the methodological process adopted by ISS ESG to evaluate corporate compliance/failure to comply with international principles (in particular, the Principles of the UN Global Compact and the OECD Guidelines for Multinational Enterprises).

55 Simone Alvaro, Marco Maugeri, and Giovanni Strampelli, 'Institutional Investors, Corporate Governance and Stewardship Codes: Problems and Perspectives' (2019), CONSOB Legal Research Papers (Quaderni Giuridici), 19.

56 Soohun Kim and Aaron Yoon, 'Analyzing Active Managers' Commitment to ESG: Evidence from United Nations Principles for Responsible Investment' (2020).

57 Option 2 proposes a minimum process and definition approach, which would provide harmonized definition relying on existing EU and international conventions. Option 3 would complement Option 2 with further specific requirements in relation to environmental issues.

58 Regulation (EU) 2020/852 of the European Parliament and of the Council of 18 June 2020 on the establishment of a framework to facilitate sustainable investment, and amending Regulation (EU) 2019/2088.

Human Rights, including the principles and rights set out in the eight fundamental conventions identified in the Declaration of the International Labour Organisation on Fundamental Principles and Rights at Work and the International Bill of Human Rights". All this means that companies should adopt a specific human rights policy, establish human rights due diligence processes, and provide a system of remedies for adverse impacts.

III. THE COMMISSION'S QUESTIONNAIRE ON DIRECTORS' DUTIES

6. Should EU company law cover directors' duties?

Some of the core questions asked by the European Commission in its consultation concern the legal treatment of directors' duties. In the Commission's view, companies' social performance should be enhanced through better specification of those duties and possibly through changes to the legal regime applicable to them under EU company law. Two preliminary questions are asked in Section I of the Consultation document. The first assumes that "due regard for stakeholder interests", such as the interests of employees, customers, etc., is expected of companies, noting that "in recent years, interests have expanded to include issues such as human rights violations, environmental pollution and climate change." The Commission asks in this regard whether 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". The question is ambiguous: one could easily agree on the premise (companies should take account of the interests of stakeholders), but not on the conclusion (EU company law should be changed to include a mandatory provision to this effect).[59]

The premise clearly reflects the "Enlightened Shareholder Value" (ESV) approach to the direction and management of companies firstly suggested by Michael Jensen and subsequently followed by the UK legislator.[60] Under this approach, corporations should take care of the interests

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[59] European Company Law Expert Group (ECLE), 'Comment by the European Company Law Experts Group on the European Commission's Consultation Document: Proposal for an Initiative on Sustainable Corporate Governance' ('2020), available at https://europeancompanylawexperts.wordpress.com/publications/comment-by-the-european-company-law-experts-group-on-the-europeancommissions-consultation-document-proposal-for-an-initiative-on-sustainable-corporate-governance/.

[60] Guido Ferrarini, 'Corporate Purpose and Sustainability' (2020), European Corporate Governance Institute - Law Working Paper 559/2020, available at SSRN: https://ssrn.com/abstract=3753594 or http://dx.doi.org/10.2139/ssrn.3753594. An edited version of this paper will be published as a chapter in Danny Busch, Guido Ferrarini and Seraina Grünewald (eds.), *Sustainable Finance in Europe* (London: Palgrave MacMillan, Forthcoming).

of stakeholders in view of long-term shareholder value maximization. The implication that the Commission would draw (imposing ESV through a mandatory provision) is however, ambiguous. Firstly, there is no specific requirement of EU law concerning the purpose of companies that a new Directive should clarify. Secondly, it is uncertain whether adding a similar requirement through a Directive would make corporate behaviour more sustainable. No doubt, ESV is widely followed by responsible companies in practice both for reputational reasons and because satisfying core stakeholders' interests generally maximizes long-term shareholder wealth. Some empirical papers on CSR already prove that being socially responsible leads companies to better financial performance or at least does not negatively affect their performance.[61] Therefore, we believe that mandating ESV would not substantially change the present situation, also considering the enforcement problems discussed below (§ 10). Thirdly, it is unclear why legislation should be adopted at EU level, rather than by the Member States under the subsidiarity principle.

There are two possible reasons for legislation on directors' duties and sustainability. One is to protect directors from liability towards the company and its shareholders when motivating corporate decisions by reference to the interests of stakeholders. The other is that company law performs an education function with respect to corporate directors and managers, leading them to take a wider account of sustainability issues.[62] Moreover, EU provisions could only be motivated by the need for a level playing field for companies in the internal market and by the willingness to control externalities across-borders. Individual Member States, however, already provide rules on either corporate purpose or the company's interest in terms that are sufficiently flexible and therefore compatible with sustainability goals.[63] Some jurisdictions (like Germany) follow multiple approaches to corporate purpose, which refers to both shareholders' and stakeholders' interests in defining corporate goals. Even jurisdictions that follow a shareholder primacy approach generally allow or require companies to consider stakeholders' interests in view of maximizing long-term profits.[64] Therefore, there is no need for EU company law to define the corporate purpose and directors' duties in ways that clarify what already seems clear at Member States' level. The need for a level playing field in the EU seems to be unjustified, given that companies tend to follow uniform

[61] See, for instance Alexander Dyck, Karl V. Lins, Lukas Roth, and Hannes F. Wagner, 'Do Institutional Investors Drive Corporate Social Responsibility? International Evidence (2018), *Journal of Financial Economics* 000, 1-22; Gunnar Friede, Timo Busch, and Alexander Bassen, 'ESG and financial performance: Aggregated evidence from more than 2000 empirical studies' (2015), *Journal of Sustainable Finance & Investment, 5*, 210–233.

[62] See Lucian A. Bebchuk and Roberto Tallarita, 'The Illusory Promise of Stakeholder Governance' (2020), *Cornell Law Review*, Forthcoming.

[63] Ferrarini, note 60.

[64] Ibidem.

practices in this area across borders.[65] Moreover, as we explain below, it is doubtful whether the specification of directors' duties can effectively control externalities.

7. Should EU company law cover due diligence requirements?

The second preliminary question posed by the Commission in Section I of its document is based on an assumption which is difficult to dispute, particularly with reference to large companies: "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". The question asks in particular whether an EU legal framework for supply chain due diligence should be developed to address adverse impacts on human rights and environmental issues. This question is connected with the wider ones included in Section III of the questionnaire concerning due diligence in general. We will not consider these specifically in this paper, as we focus on directors' duties rather than on the duties of the corporation.

For the sake of completeness, we clarify that we believe an EU legal framework for supply chain due diligence should recognise possible effects on human rights and the environment given that international standards in this area - such as the OECD Due Diligence Guidance for Responsible Business Conduct - have obtained wide approval and are already followed by many corporations in practice. EU measures of a general character could enhance the implementation of those standards by a greater number of firms and improve their engagement in sustainability matters. If a public enforcement regime were adopted, deterrence would improve compliance with the relevant standards and rules, while a level playing field would be created amongst corporations at EU level. At the same time, the OECD guidance would complement public regulation, by specifying the standards established therein. In our view, imposing due diligence duties on corporations rather than on directors is preferable for two reasons. Firstly, compliance with similar duties requires an organizational effort that firms should undertake directly at managerial level, under the supervision of the board. Secondly, corporations should face liability for breaches of those duties, while directors should only be liable for breaches of their supervisory duties in conformity with their function. Therefore, we support in principle the policy of the European Parliament to recommend the drawing up of a directive on corporate due diligence and corporate accountability.[66]

65 Ibidem.

66 European Parliament, n 9.

8. Should EU company law specify the duty of care?

The following comment introduces the questions asked in Section II of the consultation document: "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."

In our view, the reference to the duty of care is not entirely appropriate, given that the duty of loyalty is primarily at play when the directors are required to act in the company's interest.[67] Moreover, it is not true that the duty of care is not clearly defined at the Member States level. Being a general standard, its definition cannot be very specific, with the courts asked to specify it in individual cases.[68] Neither can it be said that the lack of a clear definition contributes to short-termism and to a narrow interpretation of the duty of care as requiring a focus predominantly on shareholders' financial interests. It is undisputed in most Member States that the duty of care requires directors to take stakeholders' interests into account to pursue the firm's long-term profits.[69] The sole pursuit of short-term shareholders' interest would not necessarily comply with the duty of care of directors, particularly if stakeholders' interests are ignored.[70]

Furthermore, the Commission assumptions - strongly criticized also by others -[71] ignore that several corporate governance codes in the EU not only recommend boards to maximize shareholder value in the long-term taking into account stakeholders' interest, but also encourage them to adopt CSR policies, linking the variable component of executive remuneration to CSR criteria and assigning CSR functions to a pre-existing board committee or to an ad hoc committee.

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[67] See Paul Davies, I*ntroduction to Company Law* (Oxford: Oxford University Press, 3rd ed., 2020), 179.

[68] On the choice between rules and standards in company law, see Reinier Kraakman, John Armour, Paul Davies, Paul, Luca Enriques, Henry Hansmann, Gerard Hertig, Klaus Hopt, Hideki Kanda, Mariana Pargendler, Wolf-Georg Ringe, Edward Rock, *The Anatomy of Corporate Law. A comparative and functional approach* (Oxford: Oxford University Press, 3rd ed. 2017), 32.

[69] Ibidem, 23, noting that "the corporation—and, in particular, its shareholders, as the firm's residual claimants and risk-bearers—have a direct pecuniary interest in making sure that corporate transactions are beneficial, not just to the shareholders, but to all parties who deal with the firm".

[70] See Davies, n 66, with specific reference to the Enlightened Shareholder Value approach followed by section 172 of the UK Companies Act 2006.

[71] See, for example, Roe et al., n 14.

The Luxembourgish Code, for instance, recommends the board "to serve all the shareholders by ensuring the long-term success of the company" while considering corporate social responsibility and taking the interests of all stakeholders into account in their deliberations.[72] Similarly, the Spanish code recommends that the board "in pursuing the corporate interest" should "strive to reconcile its own interests with the legitimate interests of its employees, suppliers, clients and other stakeholders, as well as with the impact of its activities on the broader community and the natural environment".[73] More specifically, it recommends the adoption of a CSR policy[74] and provides for a detailed description of the minimum content of such a policy,[75] in addition to requiring to report on corporate social responsibility developments in its directors' report or in a separate document, using an internationally accepted methodology. Like the Luxembourgish Code, the Spanish code encourages companies to identify and assign specific CSR functions to a pre-existing committee (such as the audit committee or the nomination committee) or to an ad hoc corporate governance and social responsibility committee.[76] The same Recommendation is also made by the Danish code,[77] which also recommends that the board of directors adopt policies on corporate social responsibility.[78]

9. To what extent should directors consider stakeholders' interests?

Questions 5-10 of the Commission's Questionnaire essentially ask whether the directors' duty of care should include a consideration of stakeholders' interest and to what extent company law should be modified to reflect it.

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72 The X Principles of Corporate Governance of the Luxembourg Stock Exchange (2017), Principle 2. In particular, Recommendation 2.3. states that "in defining the values of the company, the board shall take into consideration all CSR aspects of the business", while Recommendation 9.3. specifies that the board shall "regularly consider the company's non-financial risks, including in particular the social and environmental risks". In addition, the board shall "define, precisely and explicitly, the quantitative and qualitative criteria linked to the CSR aspects when determining the variable part of the remuneration of members of the Executive Management" (Recommendation 9.3, Guideline 1) and shall "set up a specialised committee to deal with CSR aspects ..." (Guideline 2).

73 (Spanish) Good Governance Code of Listed Companies (2020), Recommendation 12.

74 Ibidem Principle 24.

75 "[...] a) the goals of its corporate social responsibility policy and the support instruments to be deployed; b) the corporate strategy with regard to sustainability, the environment and social issues; c) concrete practices in matters relative to: shareholders, employees, clients, suppliers, social welfare issues, the environment, diversity, fiscal responsibility, respect for human rights and the prevention of illegal conducts; d) the methods or systems for monitoring the results of the practices referred to above, and identifying and managing related risks, e) the mechanisms for supervising non-financial risk, ethics and business conduct; f) channels for stakeholder communication, participation and dialogue; g) responsible communication practices that prevent the manipulation of information and protect the company's honour and integrity": ibidem, Recommendation 54.

76 Ibidem Principle 23 and Recommendation 53.

77 (Denmark) Recommendations on Corporate Governance (2019), Recommendation 3.4.

78 Ibidem, Recommendation 2.2.

(i) Question 5 asks respondents to identify which stakeholders' interests are "relevant for the long-term success and resilience of the company", while Question 6 invites them to consider whether "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". We believe that already today, directors of well-run companies should identify the company's stakeholders and manage their risks with respect to them. This is generally suggested by management theory, best practices and protecting corporate reputation, as in the case of the materiality assessment required for sustainability reporting.[79] Moreover, directors of "good" companies already consider the business opportunities which arise from promoting stakeholders' interests, often under a "shared value" approach.[80] In fact, the pursuit of stakeholders' interests can be combined with long-term value maximization in ways that increase the pie's total size (which is made of corporate profit and the social value created by the firm). However, this should not be strictly mandated by the law, for the simple reason that similar outcomes can be reached by the managers through the exercise of their business judgement, with the flexibility allowed by the application of a legal standard like the duty of care. Mandating the pursuit of "shared value" in precise terms would bureaucratize managerial conduct, which would in most cases escape enforcement of the relevant provisions given the general applicability of the business judgement rule.

Some codes of corporate governance already include provisions on the treatment of stakeholders' interests. Our previous Study found that 20 out of 27 corporate governance codes mention stakeholders, with 12 of them also including a more or less detailed definition of them.[81] Most of the definitions provided (for example by the Luxembourgish and Greek codes) refer to the OECD Principles' definition of stakeholders and specify the interest groups that fall under it (employees, clients, investors, suppliers, local community, and regulators). Other codes (such as the Bulgarian and Dutch ones) mention the concept of reciprocal, direct and indirect "influence" between the company and such groups. In addition, the codes from Bulgaria, Croatia, Lithuania, Slovakia and Slovenia include an entire chapter describing the duties of the company towards its stakeholders. More specifically, in different combinations, all the codes just cited recommend the

79 Directive 2013/34/EU of the European Parliament and of the Council of 26 June 2013 on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings, Article 2(16). In this regard, we are considering, among others, the materiality assessment that companies should perform when adopting the GRI reporting standards - which are the most frequently adopted standards for sustainability reporting - for their non-financial disclosure activities.

80 See M. Porter and M. Kramer, 'Creating Shared Value: How to Reinvent Capitalism – and Unleash a Wave of Innovation and Growth' (2011) Harvard Business Review 3.

81 Siri & Zhu, n 2.

board to : (1) identify the stakeholders who are in the position to influence and impact the company's sustainable development;[82] (2) comply with existing laws protecting stakeholders' rights;[83] (3) ensure transparency and access to information through constant dialogue and non-financial disclosure;[84] (4) ensure that stakeholders can freely communicate their concerns about illegal or unethical practices to the board;[85] (5) promote stakeholder participation in corporate decisions (such as employee participation in certain key decisions and/or in the company's share capital; creditor involvement in the governance in the context of the company's insolvency etc.);[86] (6) report on the board's relationships with stakeholders.[87]

On the whole, corporate governance codes that already follow an ESV approach encourage corporate boards to take stakeholders' interests into account. However, only a minority of the codes further specify to what extent such interests should be served by offering a detailed description of the duties of the board towards company stakeholders.

(ii) Question 7 of the Consultation document further asks whether "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, i.e. human rights, social, health and environmental impacts are identified, prevented and addressed". Large corporations are already moving in this direction and include stakeholders in their risk management systems. This is done to reduce both stakeholders' risks to the company, including reputational risks, and the company's negative impacts on the environment and society, as widely recommended by the international documents cited above. The provision suggested by the Commission as a possible addition to EU company law is consistent with the guidance offered by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) and the World Business Council for Sustainable Development (Wobcsd) in a document[88] designed to apply to COSO's

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82 (Bulgarian) National Corporate Governance Code (2016), §38.

83 Ibidem, §39; The (Lithuanian) Corporate Governance Code for the Companies Listed on NASDAQ OMX Vilnius (2010), Principe 9.1.; (Croatian) Corporate Governance Code (2019), p. 23; Corporate Governance Code for Slovakia (2016), 17.

84 (Bulgarian) National Corporate Governance Code (2016), §42-43, (Czech) Corporate Governance Code based on the OECD Principles (2004), p.18; The (Lithuanian) Corporate Governance Code for the Companies Listed on NASDAQ OMX Vilnius (2010), Principle 9.3; Slovenian Corporate Governance Code For Listed Companies (2016), p. 8; The (Maltese) Code Of Principles Of Good Corporate Governance, Principle 4.

85 Corporate Governance Code for Slovakia (2016), p. 18, (Czech) Corporate Governance Code based on the OECD Principles (2004), 18

86 The (Lithuanian) Corporate Governance Code for the Companies Listed on NASDAQ OMX Vilnius (2010), Principle 9.2, Corporate Governance Code for Slovakia (2016), p. 17; Slovenian Corporate Governance Code for Listed Companies (2016), 8.

87 Slovenian Corporate Governance Code for Listed Companies (2016), 8.

88 COSO and WOBCSD, 'Enterprise Risk Management. Applying enterprise risk management to environmental, social and governance-related risks' (2018).

enterprise risk management (ERM) framework[89] and addressing the need for companies to integrate environmental, social and governance-related risks (ESG) into their ERM processes. The guidance notes that over the last 10 years the prevalence of ESG-related risks has accelerated rapidly: "In addition to a clear rise in the number of environmental and social issues that entities now need to consider, the internal oversight, governance and culture for managing these risks also require greater focus."[90] The World Economic Forum reported that for 2018 four of the top five risks were environmental or societal, including extreme weather events, water crises, natural disasters, and failure of climate change mitigation and adaptation.[91] In 2020 all five top risks were environmental, including extreme weather, climate action failure, natural disasters, biodiversity loss and human-made environmental disasters.[92]

Given that best practice is already oriented in the sense of including ESG-related risks in the ERM process and that detailed guidance is provided in this regard, which naturally fits with the duty of care of directors, we doubt that the provision suggested in Question 7 would add much value to what is already the law in practice. We also doubt that an EU provision is needed, given that the member States can better choose whether to clarify the director's duties in through either company law or a corporate governance code. They can also choose to what extent the relevant provisions or recommendations should refer to the international documents and guidance considered above.

(iii) Question 8 is tricky as it asks whether "corporate directors should balance the interests of all stakeholders, instead of focusing on the short-term financial interests of shareholders, and [whether] this should be clarified in legislation as part of directors' duty of care".[93] However, asking to choose between "balancing the interests of all stakeholders" and "focusing on the short-term financial interests of shareholders" is misleading. A balance of the gamut of stakeholders' interests should be reached that is subsequently balanced with those of shareholders, which are not necessarily short-term oriented. The corporation should pursue a profit goal and satisfy the interests of shareholders to the extent necessary to reach this goal. A provision such as the one suggested could imply that the interests of stakeholders always prevail over the short-term interests of shareholders. Nevertheless, short-term shareholder interests should not always be set aside, for there are cases in which they also deserve protection. For example, temporarily blocking salary increases could help achieve short-term financial targets to enable employees and shareholders to

89 COSO, 'Enterprise Risk Management—Integrating with strategy and performance' (2017).
90 Ibidem, 2.
91 World Economic Forum, The Global Risks Report, 2018, Figure 1.
92 Ibidem.
93 Question 9 similarly asks what the risks of the duty of care are as described in question 8.

subsequently divide a larger pie amongst themselves. In general, directors should identify and reconcile the range of stakeholders' interests and balance these with those of shareholders to pursue long-term financial gains.

(iv) Question 10 assumes that "companies often do not have a strategic orientation on sustainability risks, impacts and opportunities" asking "whether such considerations should be integrated into the company's strategy, decisions and oversight within the company". We believe that sustainability issues, including non-financial reporting, should be integrated into the firm's direction and management. Therefore, the firm's strategies and its risk management systems should take sustainability issues into account. Also, decision made by the board of directors should take into account stakeholders' interest. We see no objection to company law recognizing explicitly the need to integrate sustainability considerations in the firm's direction and leadership, except that this could also be provided to some extent by corporate governance codes rather than by legislation. The Swedish code, for instance, among the main duties of the board of directors, already includes the task of "identifying how sustainability issues impact risks to and business opportunities for the company".[94]

10. **Enforcement of directors' duties**

The subsequent questions in the Commission's document are headed "Enforcement of directors' duty of care" and are introduced by the following statement: "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." Reference is implicitly made here to the liability actions against directors and managers promoted either by the board of directors, the supervisory board or the shareholders' meeting.[95] Derivative suits should also be considered, which can be brought by the shareholders on behalf of the company in some national systems, including the Italian one.[96] The Commission assumes that the limits within which

[94] The Swedish Corporate Governance Code (2020), Principle 3.2.

[95] Martin Gelter, 'Mapping Types of Shareholder Lawsuits Across Jurisdictions', in Jessica Erickson, Sean Griffith, David Webber and Verity Winship (eds) *Research Handbook on Shareholder Litigation* (Elgar, 2018).

[96] See Paolo Giudici, 'Representative Litigation in Italian Capital Markets: Italian Derivative Suits and (if ever) Securities Class Actions' (2009), *European Company and Financial Law Review*, 246.

liability suits can be brought in the national systems have contributed to the narrow interpretation of the duty of care under which directors supposedly perform their duty by acting in the company's short-term interest. To our knowledge, a similar thesis has never been advanced by scholars, who argue instead that liability suits for breaches of the duty of care are rare in the Member States as a consequence of the business judgment rule[97] and other hurdles created by the law of civil procedure particularly in the area of discovery, in addition to high costs of litigation and lack of incentives.[98] Derivative suits could no doubt ease the enforcement of the duty of care provided that the hurdles deriving from civil procedure rules are overcome.[99]

In light of the above, the narrow interpretation of the duty of care which the Commission laments has little to do with the low rate of liability litigation brought by shareholders in Europe. Moreover, the business judgement rule rightly protects directors to the extent that it is difficult to ground civil liability claims, as this would deter efficient risk-taking[100] and courts generally do not possess adequate expertise to make a proper evaluation of business decision-making.[101] In Question 13 the Commission asks, in particular, whether stakeholders and third parties, in general, should be given enforcement rights, specifically referring to stakeholders, such as for example employees, the environment or people affected by the operations of the company as represented by civil society organisations." In our view, only shareholders should be entitled to bring a derivative suit for breaches of the duty of care for the simple reason that the directors act on their behalf and in the interest of the company. Stakeholders are nonetheless entitled to bring an action against the company for breaches of the rules protecting them, for instance, in the area of environmental protection. There are no reasons for allowing stakeholders to bring either direct action or a derivative suit against the directors for breaches of the duty of care which directors owe directly to the company.

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97 See Holger Spamann, 'Monetary Liability for Breach of the Duty of Care?' (2016), *Journal of Legal Analysis*, 8, (2).

98 See Martin Gelter, 'Why do Shareholder Derivative Suits Remain Rare in Continental Europe?' (2012), *Brooklyn Journal of International Law*, 37(3); Giudici, n 93; Mathias Siems, 'Private Enforcement of Directors' Duties: Derivative Actions as a Global Phenomenon', in Stefan Wrbka, Steven Van Uytsel and Mathias Siems (eds.) *Collective Actions: Enhancing Access to Justice and Reconciling Multilayer Interests?* (Cambridge: Cambridge University Press, 2012), 93-116; Michael D. Klausner, 'The Limits of Corporate Law in Promoting Good Corporate Governance' (2004).

99 According to Gelter, n 96, we should consider four necessary requirements in the absence of which derivative suits could with difficulty be promoted in certain jurisdictions: (i) the absence of a minimum ownership threshold to stand, (ii) a favourable allocation of litigation risks to overcome minority shareholders' rational apathy; (iii) availability of information to potential plaintiffs; and (iv) the possibility to derivatively sue potential wrongdoers, which not only includes directors, but also controlling shareholders.

100 Bernard Black, Brian Cheffins, and Michael Klausner, 'Outside Director Liability: A Policy Analysis' (2006), *Journal of Institutional and Theoretical Economics,* 5; Spamann, n 95.

101 Bernard S. Sharfman, 'The Importance of the Business Judgment Rule' (2017), *New York University Journal of Law and Business*, 27.

IV. THE BROADER CONTEXT

11. Recent reforms of EU company law regarding short-termism

Even assuming the existence of widespread short-termism in managerial actions, reforming directors' duties does not seem to be the most effective way to control such a phenomenon. Other reforms may be more effective such as those concerning the incentives of corporate executives as to the environmental and social performance of their companies. EU corporate law already includes similar rules regarding corporate managers, asset managers (whether UCITS or AIFM) and institutional investors (insurance companies and pension funds) (SRD II). Moreover, it includes provisions aimed to stimulate the engagement of institutional investors in their portfolio companies, while other measures will be likely proposed by the Commission to amend investment services regulation (MiFID II and implementing measures) so as to take sustainability factors and risks into account. Furthermore, EU company law aims to improve companies' social transparency and performance through legislation and soft law initiatives such as the Non-financial Reporting Directive (NFRD),[102] the Regulation on sustainability-related disclosures in the financial services sector (SFDR),[103] and the Regulation providing a common EU Taxonomy for sustainable financial products. In this Section, we offer an overview of the relevant EU framework.

(i) *SRD II.* In May 2017, the European Parliament and Council agreed to amend the 2007 Shareholder Rights Directive to enhance the stability and sustainability of EU companies.[104] SRD II is aimed to strengthen the engagement of shareholders and to ensure that decisions are taken for the long-term sustainability of a company. It, therefore, establishes specific requirements to encourage long-term shareholder engagement, enhance the transparency of the investment chain and align the investment strategies and remuneration structures of asset managers with the medium-to-long term performance of their investors' assets. The goal of curbing short-termism is clearly expressed by the SRD II in Recital 2, stating: "engagement by institutional investors and asset managers is often inadequate and focuses too much on short-term returns, which may lead to suboptimal corporate governance and performance". Throughout the entire Directive, the

[102] Directive 2014/95/EU on disclosure of non-financial and diversity information.

[103] Regulation (EU) 2019/2088 of the European Parliament and of the Council of 27 November 2019 on sustainability-related disclosures in the financial services sector.

[104] Directive 2007/36/EC, as amended by Directive (EU) 2017/828 as regards the encouragement of long-term shareholder engagement.

expression "long-term" is used more than 36 times, often combined with the words "performance", "approach", "interests" and "risks".

Specifically, the Directive requires institutional investors and asset managers to annually disclose their voting policy and how they have implemented it by engaging with individual companies with particular regard to their social and environmental impact and corporate governance.[105] As to executive remuneration, Article 9a of SRD II requires the remuneration policy to contribute to the company's business strategy and long-term interests and sustainability while indicating the non-financial performance criteria on which variable remuneration is based, such as those relating to corporate social responsibility.[106] Article 9b provides that the remuneration report shall explain how the total remuneration complies with the adopted remuneration policy, including how it contributes to the company's long-term performance.

What distinguishes SRD II from other soft-law measures promoting long-term engagement and stewardship[107] is the inclusion, under Article 14b, of provisions enabling Member States to introduce sanctions for the breach of the Directive's semi-hard engagement rules, as done by several countries, including Italy, Greece, the Netherlands, and France.[108]

(ii) *MiFID II, IDD, UCITS and AIFMD.* Following the publication of the European Commission's Action Plan on Sustainable Finance in March 2018, a flurry of EU legislative proposals was initiated aiming to integrate sustainability concerns in the EU financial services regulatory framework. Based on ESMA technical advice,[109] the European Commission published

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105 SRD II, Article 3g(1)(a). If it is true that in the U.S. transparency requirements concerning voting policies and behaviour should be followed by institutional investors, it should be highlighted that there is no reference to the impact on sustainability-related issues. See Pacces, n 16.

106 Moreover, the Commission Guidelines on the standardised presentation of the remuneration report under Directive 2007/36/EC suggest that, where applicable, companies should present in the remuneration report for each director a description of the financial and non-financial (including, where appropriate, corporate social responsibility) performance criteria as included in the remuneration policy. See Communication from the Commission, Guidelines on the standardised presentation of the remuneration report under Directive 2007/36/EC, as amended by Directive (EU) 2017/828 as regards the encouragement of long-term shareholder engagement.

107 Consider, for instance, the diffusion of stewardship codes. See Mark Fenwick and Erik P.M. Vermeulen, 'Institutional Investor Engagement: How to Create a 'Stewardship Culture' (2018), Lex Research Topics in Corporate Law & Economics Working Paper No. 2018-1, TILEC Discussion Paper No. 2018-006, Available at SSRN: https://ssrn.com/abstract=3098235 or http://dx.doi.org/10.2139/ssrn.3098235; Alvaro et al., n 55.

108 See Dionysia Katelouzou and Konstantinos Sergakis, 'Shareholder Stewardship Enforcement' (2020). An edited version of the paper will be published as a chapter in Dionysia Katelouzou & Dan W. Puchniak (eds) *Global Shareholder Stewardship: Complexities, Challenges and Possibilities* (Cambridge: Cambridge University Press, Forthcoming).

109 See ESMA, 'Final Report. ESMA's technical advice to the European Commission on integrating sustainability risks and factors in MiFID II' (30 April 2019); and ESMA, 'Final Report. ESMA's technical advice to the European Commission on integrating sustainability risks and factors in the UCITS Directive and AIFMD' (30 April 2019).

on 8 June 2020 a set of draft delegated acts under MiFID II,[110]IDD,[111] the UCITS Directive[112] and the AIFM Directive,[113] seeking to integrate sustainability risks and factors in organizational requirements, disclosure requirements, suitability assessment and product governance. In particular, a draft delegated Directive (to amend Commission Directive 2010/43 implementing certain provisions of the UCITS Directive) [114] and a draft delegated regulation (to amend Commission Regulation 231/2013 implementing certain AIFM Directive provisions)[115] clarify the duties of investment fund managers to take into account the social and environmental factors and risks in their governance, organisation, conflicts of interest policies, investment due diligence and risk policies and procedures. Two other delegated acts (amending those which implement the MiFID II requirements on product governance, organisational requirements, and the functioning of investment firms and those implementing IDD requirements)[116] require investment and insurance firms to integrate their clients' sustainability preferences in the investment objectives, risk profile, and capacity for loss bearing.

[110] Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Directive 2002/92/EC and Directive 2011/61/EU (MiFID II).

[111] Directive (EU) 2016/97 of the European Parliament and of the Council of 20 January 2016 on insurance distribution (IDD).

[112] Directive 2014/91/EU of the European Parliament and of the Council of 23 July 2014 amending Directive 2009/65/EC on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS) as regards depositary functions, remuneration policies and sanctions (UCITS V).

[113] Directive 2011/61/EU of the European Parliament and of the Council of 8 June 2011 on Alternative Investment Fund Managers and amending Directives 2003/41/EC and 2009/65/EC and Regulations (EC) No 1060/2009 and (EU) No 1095/2010 (AIFMD).

[114] Commission Delegated Directive (EU) .../… amending Directive 2010/43/EU as regards the sustainability risks and sustainability factors to be considered for Undertakings for Collective Investment in Transferable Securities (UCITS).

[115] Commission Delegated Regulation (EU) …/... amending Delegated Regulation (EU) No 231/2013 as regards sustainability risks and sustainability factors to be taken into account by Alternative Investment Fund Managers

[116] See Commission Delegated Regulation (EU) …/... of XXX amending Delegated Regulation (EU) 2017/565 as regards the integration of Environmental, Social and Governance (ESG) considerations and preferences into the investment advice and portfolio management; and COMMISSION DELEGATED REGULATION (EU) …/... of XXX amending Delegated Regulation (EU) 2017/2358 and Delegated Regulation (EU) 2017/2359 as regards the integration of sustainability factors and preferences into the product oversight and governance requirements for insurance undertakings and insurance distributors and into the rules on conduct of business and investment advice for insurance-based investment products.

(iii) *NFRD*. Directive 2014/95/EU on disclosure of non-financial and diversity information ('Non-financial Reporting Directive' or NFRG)[117] requires certain large companies[118] to disclose information about their due diligence processes and policies in relation to environmental, social and employee matters, respect of human rights, anti-corruption and bribery issues, and diversity on company boards (in terms of age, gender, educational and professional background). The upcoming revision of such Directive,[119] deemed necessary in light of the criticism raised, especially in relation to the lack of a minimum requirement for mandatory third-party verification[120] and other limits in practice,[121] should further increase corporate commitment to sustainability and transparency by requiring, amongst others: the adoption of a common reporting standard, so as to allow comparability, reliability and relevance; the imposition of stronger audit requirements; the digitalization of non-financial information that would become available through a single access point and machine-readability; the requirement on companies to disclose their materiality assessment process; the expansion of the scope of the Directive to a larger number of companies; and the alignment of environmental disclosure with the EU taxonomy.[122]As mentioned above (§2), the upcoming Directive on corporate due diligence and corporate accountability will complement this framework, by requiring undertakings (both large and SMEs) to comply with due diligence

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117 In accordance with Article 2 of the same directive, in 2017 the EU Commission published some voluntary guidelines on methodology for reporting non-financial information in order "to help companies disclose high quality, relevant, useful, consistent and more comparable non-financial information in a way that fosters resilient and sustainable growth and employment, and provides transparency to stakeholders". The EU Commission further integrated such guidelines to improve the corporate disclosure of climate-related information in line with recommendations made by the EU Technical Expert Group on Sustainable Finance. European Commission. See Guidelines on non-financial reporting 2017/C 215/01 and European Commission. Guidelines on Non-Financial Reporting: Supplement on Reporting Climate-Related Information, C (2019) 4490 Final (17 June 2019). Available online: https://ec.europa.eu/finance/docs/policy/190618-climate-related-information-reporting-guidelines_en.pdf).

118 This directive applies, specifically, to "large undertakings which are public-interest entities exceeding on their balance sheet dates the criterion of the average number of 500 employees during the financial year. See Article 19a of the Non-Financial Reporting Directive.

119 See https://ec.europa.eu/info/law/better-regulation/have-your-say/initiatives/12129-Revision-of-Non-Financial-Reporting-Directive/public-consultation. See Commission, 'Consultation strategy for the revision of the Non-Financial Reporting Directive – Background document' (20 February 2020).

120 Recital 16 of the Non-Financial Reporting Directive requires that 'statutory auditors and audit firms should only check that the non-financial statement or the separate report has been provided' and leaves to the Member States the discretionary power to 'require that the information included in the non-financial statement or in the separate report be verified by an independent assurance services provider'. The lack of mandatory third-party verification of non-financial statements reduces their reliability level. See Siri & Zhu, n 6.

121 Empirical research found that non-financial statements are generally affected by lack of quantitative disclosure, lack of clarity concerning the selection and measurability of non-financial targets, but also that they are over-generic, they do not appropriately address climate-related risks nor provide sufficient descriptions of due diligence processes, especially related to human rights and social matters. See ESMA, 'Report Enforcement and regulatory activities of European enforcers in 2019' (2020) and Alliance for Corporate Transparency, 'Research Report: An analysis of the sustainability reports of 1000 companies pursuant to the EU Non-Financial Reporting Directive' (2020).

122 See EU Commission, Summary Report of the Public Consultation on the Review of the Non-Financial Reporting Directive, Ares(2020)3997889 - 29/07/2020, available at https://ec.europa.eu/info/law/better-regulation/have-your-say/initiatives/12129-Revision-of-Non-Financial-Reporting-Directive/public-consultation.

obligations in order to consider and better address the actual or potential adverse impact of their activities on human rights, the environment or good governance.

(iv) *Taxonomy Regulation*. The establishment of a common sustainable finance taxonomy was the first key in the HLEG final report,[123] which found acceptance on 18 June 2020 when the European Parliament and the Council adopted the Regulation (EU) 2020/852 "on the establishment of a framework to facilitate sustainable investment and amending Regulation (EU) 2019/2088 ('Taxonomy Regulation').[124] The Taxonomy Regulation, along with Regulation (EU) 2019/2088 on sustainability-related disclosures in the financial services sector" ('Sustainable Finance Disclosure Regulation' or SFDR) and Regulation (EU) 2019/2089 on EU Climate Transition Benchmarks, EU Paris-aligned Benchmarks and sustainability-related disclosures for benchmarks (the 'Low Carbon Benchmarks Regulation'), implement the Commission Action Plan "on Building a Capital Markets Union" (CMU) as to sustainable finance.

The Taxonomy Regulation establishes a classification system of environmentally sustainable economic activities at Union level to be used as the basis for other economic and regulatory measures, with the aim of facilitating the shift of investment towards environmentally sustainable economic activities, by increasing the reliability, consistency and comparability of sustainability-related disclosures in the financial services sector.[125] Due to the complexity of developing a full classification system covering both environmental and social aspects, the Commission decided to approach, in a first step, only the environmental activities contributing to the 6 environmental objectives defined in Article 9 of the Taxonomy Regulation: (i) climate change mitigation, (ii) climate change adaptation, (iii) sustainable use and protection of water and marine resources, (iv) transition to a circular economy, waste prevention and recycling, (v) pollution prevention and control, and (vi) protection of healthy ecosystems. The Taxonomy Regulation and the related Commission delegated acts[126] will have an impact on both portfolio choices of institutional investors and on the corporate governance of the investee companies. They will help to prevent

[123] HLEG, Final Report (2018). Available online: https://ec.europa.eu/info/sites/info/files/180131-sustainable-finance-final-report_en.pdf.
[124] See Christos Gortsos, 'The Taxonomy Regulation: More Important Than Just as an Element of the Capital Markets Union' (2020), European Banking Institute Working Paper Series 2020 N. 80, Available at SSRN: https://ssrn.com/abstract=3750039 or http://dx.doi.org/10.2139/ssrn.3750039.
[125] Taxonomy Regulation, Recitals 15-16.
[126] The Draft Delegated Act on climate change mitigation and climate change adaptation was published on November 20, containing a draft Delegated Regulation, Annex I on the climate change mitigation environmental objective and Annex II on the climate change adaptation objective; available at: https://ec.europa.eu/info/law/betterregulation/have-your-say/initiatives/12302-Climate-change-mitigation-and-adaptationtaxonomy#ISC_WORKFLOW.

the 'greenwashing' practices of companies, increase the reliability and comparability of non-financial information, and contribute to curbing short-termism.

(v) *Sustainable Finance Disclosure Regulation (SFDR).* Regulation (EU) 2019/2088 of 27 November 2019 on sustainability-related disclosures in the financial services sector aims to reduce information asymmetries in principal-agent relationships with regard to the integration of sustainability risks, the consideration of adverse sustainability impacts, the promotion of environmental or social characteristics, and sustainable investment, by requiring financial market participants and financial advisers to make pre-contractual and ongoing disclosures to end-investors when they act as agents of those end-investors (principals).[127]

The SFDR requires financial markets participants[128] and financial advisers to publish on their websites and include in their pre-contractual documents information on their policies as to the integration of sustainability risks in their investment decision-making processes and in their investment or insurance advice,[129] explaining whether (and if not, why) they consider the adverse impacts of investment decisions on sustainability factors and the consistency of remuneration with sustainability risk inclusion.[130] Both financial market participants and financial advisers should also include in their remuneration policies information on how those policies are consistent with the integration of sustainability risks, and publish that information on their websites.[131] Additional information shall be published in the event that a financial product promotes, among other characteristics, environmental or social characteristics, or a combination of those characteristics, and in the event that a financial product has sustainable investment as its objective and an index has been designated as a reference benchmark.[132] Moreover, pursuant to Article 5-8 of the Taxonomy Regulation, where a financial product is marketed for its environmental characteristics, the disclosure should include information on how those characteristics are also met in relation to the EU Taxonomy and, where a product does not qualify as "sustainable investment", pre-contractual disclosure and period reports must contain a disclaimer specifying that the investments underlying this financial product do not take into account the EU criteria for environmentally sustainable economic activities.

127 Recital 10, SFDR.
128 These include, among others, portfolio managers, managers of UCITS, AIF or EuVEC/EuSEF, IORP and pension product manufacturer, PEPP providers. See Article 2(1), SFDR.
129 Articles 3, 6 and 7, SFDR.
130 Article 4, SFDR.
131 Article 5(1), SFDR.
132 Articles 8-9, SFDR.

On 2 February 2021 the ESAs published a final report containing draft regulatory technical standards (RTS) on the content, methodologies and presentation of sustainability-related disclosures under Articles 2a, 4(6) and (7), 8(3), 9(5) and 10(2) and 11(4) of the Sustainable Finance Disclosure Regulation.[133] Even though the comply or explain approach and other limitations could negatively impact the full harmonization of sustainability-related disclosure rules and fiduciary duties across Member States,[134] the SFDR will contribute to the need for more detailed and reliable ESG information, which eventually means pushing companies to be more transparent in their efforts to integrate a sustainable and long-term approach to their business practices, especially in view of the marketing difficulties for financial products that do not claim to achieve any degree of sustainability .[135]

V. CONCLUSIONS

In this paper, we have examined whether EU company law should be reformed to make corporate governance more sustainable through an analysis of some of the key questions included in the questionnaire submitted by the European Commission to consultation.[136] Adding to the important criticism raised by academics and stakeholders, we have argued that the Commission has paid scant attention to the role of corporate governance codes and other soft law instruments of international origin. Moreover, we have shown that many of the consultation questions already find an answer either in corporate governance codes or in international company law. Undoubtedly, the lack of homogeneity between the codes and their weak implementation and enforcement in practice may suggest that they are not entirely fit to respond to the need for sustainable corporate practices. However, the principles and guidelines issued by international organizations and standard setters (including the IMF, the OECD, the World Bank, and the United Nations) contribute to filling this gap and establishing new standards of corporate behaviour to reduce the negative impact of corporate activities on third parties. In a similar context, compliance with the international principles and standards is more common today, considering that companies respond to investors' growing attention to the ESG performance of their portfolio companies.

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133 Available at https://www.eba.europa.eu/three-european-supervisory-authorities-publish-final-report-and-draft-rts-disclosures-under-sfdr.

134 See Danny Busch, 'Sustainability Disclosure in the EU Financial Sector' (2020), European Banking Institute Working Paper Series 2020 - n. 70, available at SSRN: https://ssrn.com/abstract=3650407 or http://dx.doi.org/10.2139/ssrn.3650407.

135 Ibidem.

136 See European Commission, n. 1.

Moreover, we have shown that national company laws as to fiduciary duties are already aligned with the need for companies to maximize long-term shareholder wealth, also taking the interests of stakeholders into account, while the short-termism lamented by the Commission does not appear to be promoted or tolerated by the same laws and their interpretation in practice. We have also rejected the thesis that corporate short-termism may be generated by the lack of enforcement of fiduciary duties and by the rarity of cases in which corporate directors have been found liable. Indeed, the business judgement rule rightly protects directors from the risk of being held liable by the courts judging with the benefit of hindsight, always provided that directors have acted in good faith and duly informed about the relevant circumstances.

Furthermore, we have argued that the broader context of EU company law should be thoroughly considered. Several reforms have been adopted by the EU legislature in recent years, such as the Non-Financial Disclosure Directive, the Taxonomy Regulation, the Sustainable Finance Disclosure Regulation and the Shareholder Rights Directive II, which address corporate short-termism and try to promote sustainability in the governance of firms. They offer better prospects for sustainable governance than the reform of directors' duties that the Commission is planning. Focussing on the full implementation and enforcement of the reforms already made would be for the Commission a better choice than further amending company law in the direction examined throughout this paper.

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