ShareAction»

EU Sustainable Corporate Governance Consultation Summary

ShareAction, the responsible investment advocacy group, welcomes the opportunity to provide feedback to this consultation on sustainable corporate governance. Significant changes to the dominant economic and business model, which is based on infinite growth and prioritising short-term profits, are urgently needed. Companies need to elevate and protect the interests of all stakeholders to develop a more balanced approach where the interests of key groups are meaningfully taken into account. We therefore strongly support the Commission's efforts to enable companies to focus on long-term sustainable value creation, to better align the interests of companies, their shareholders, managers, stakeholders and society and to help companies to better manage sustainability-related matters.

Our main recommendations are:

1. **Establish a legal duty for companies to undertake environmental and human rights due diligence.**
   - Mandatory due diligence legislation is needed to integrate environmental and human rights impacts into corporate decision-making. It would furthermore ensure high quality ESG data is provided to investors by corporates, which allows responsible investors to drive sustainable corporate change through stewardship and engagement.
   - The requirements should be applicable to all sectors, including the financial industry. ShareAction's research shows that many financial institutions do not sufficiently take environmental and social factors into consideration. It is therefore of utmost importance that the forthcoming legislation includes all financial institutions in the scope of due diligence obligations, thereby preventing the financial industry from disregarding their adverse impacts on environment and human rights and seeking to prevent or mitigate these within their operations.

2. **Clarify directors' duties to ensure that the sustainability matters are duly considered at a strategic level and put forward transparently in the company's overall strategy.**
   - The initiative should clarify the responsibilities of directors to oversee and ensure the quality implementation of the due diligence and materiality determination processes, and to adopt, disclose and ensure implementation of a forward-looking sustainability strategy and targets based on the findings of these processes.
   - An expanded definition of directors' duty of care needs to be complemented with the necessary enforcement and implementation mechanisms against a backdrop of ever-decreasing direct ownership, short share-holding periods and issues with the exercise of voting rights. In order to counter remuneration incentivizing short-term focus, it is important to not only link variable remuneration to non-financial performance but to also withhold variable remuneration that motivate economic activities with material adverse impacts (e.g., oil executives remunerated according to oil production and exploration metrics).

3. **Strengthen directors' duties towards stakeholder interests.**
    - The growing diversification and interconnectedness of the world in which companies operate means that if they are to navigate growing systemic uncertainty, directors must understand the purpose and impact of the company they lead, and to do this they must listen to stakeholders affected by the activities of the company.
    - An example of how stakeholder engagement can be improved is through Annual General Meetings (AGMs). AGMs should create a purposeful ongoing process through which they will gather insight from stakeholders, this can be done by:
        - ensuring the AGM is a process of engagement with stakeholder groups throughout the year.
        - organising the AGM event as a meeting focusing on how directors' have fulfilled their responsibility to stakeholders. Shareholders will be able to hear, challenge and discuss the views of stakeholders impacted by corporate activity, including any issues on directors' duty of care.

More detailed recommendations can be found in response to the consultation questions below and draw on ShareAction's research and expertise.

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About ShareAction

ShareAction is a non-profit working to build a global investment sector which is responsible for its impacts on people and planet. We mobilise investors to take action to improve labour standards, tackle the climate crisis, and address pressing global health issues, such as childhood obesity. Over the last 15 years, ShareAction has used its powerful toolkit of research, corporate campaigns, policy advocacy and public mobilisation to drive responsibility into the heart of mainstream investment. We want a future where all finance powers social progress.

ShareAction's EU policy engagement focuses on supporting the development of an effective regulatory framework of sustainable finance and long-term investment that ensures the interests of end-investors are heard and the financial sector helps deliver on ambitious environmental and social goals.

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Consultation for an Initiative on Sustainable Corporate Governance – CSO response template

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

Question 1: Due regard for stakeholder interests', such as the interests of employees, customers, etc., is expected of companies. In recent years, interests have expanded to include issues such as human rights violations, environmental pollution and climate change.

Do you think companies and their directors should take account of these interests in corporate decisions alongside financial interests of shareholders, beyond what is currently required by EU law?

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

Please provide reasons for your answer:
Companies and their directors should take environmental, social and governance issues into account and it is critical that legislative and regulatory provisions require this. Despite growing awareness of the elements of responsible business conduct, companies have not fundamentally changed the way they do business. The law should clarify the responsibilities of directors to oversee and ensure quality implementation of the due diligence and materiality determination processes, and to adopt, disclose and ensure implementation of a forward-looking sustainability strategy and targets based on the findings of these processes.

Significant changes to the dominant economic and business model, which is based on infinite growth and prioritising short-term profits, are urgently needed. It is not acceptable for companies to benefit from societal stability while undermining it at the same time. Companies need to elevate and protect the interests of all stakeholders to develop a more balanced approach where the interests of key groups - including workforce, supply chain workers, indigenous peoples, affected communities and human rights, environmental and land defenders - are meaningfully taken into account.

The corporate responsibility to address impacts may be relevant to the financial performance of the company in the long-term. The impact of social and environmental matters on companies' financial performance, as well as the question of whether companies should maximise their social and environmental performance, is relevant in its own right and should be considered in the reform of corporate governance. The South African King IV Code expresses this recognition in the following terms: "The company is represented by several interests and these include the interests of shareholders, employees, consumers, the community and the environment. Thus, requiring directors to act in good faith in the interest of 'the company' cannot nowadays mean anything other than a blend of all these interests, but first and foremost they must act in the best interest of the company as a separate legal entity. Any interest that may be primary at one particular point in time in the company's existence may well become secondary at a later stage."

The strong pressures from outside company law mean the problem of short-termism cannot be solved simply by requiring or permitting directors to have regard to sustainability and the company's long-term interest, or by facilitating or mandating other stakeholders' engagement in corporate governance. Instead, the law should clarify the responsibilities of directors to oversee and ensure the quality implementation of the due diligence and materiality determination processes, and to adopt, disclose and ensure implementation of a forward-looking sustainability strategy and targets based on the findings of these processes. The purpose of such clarification is to ensure that the sustainability matters are duly considered at a strategic level and put forward transparently in the company's overall strategy. This would provide investors and other stakeholders with information enabling them to meaningfully engage with the company in accordance with law, rather than impose any new behavioural obligation or change corporate governance system.

Question 2: Human rights, social and environmental due diligence requires companies to put in place continuous processes to identify risks and adverse impacts on human rights, health and safety and environment and prevent, mitigate and account for such risks and impacts in their operations and through their value chain.
In the survey conducted in the context of the study on due diligence requirements through the supply chain, a broad range of respondents expressed their preference for a policy change, with an overall preference for establishing a mandatory duty at EU level.

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

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

Please explain:
If left to voluntary market action, current due diligence measures will not sufficiently integrate environmental and human rights impacts into corporate decision-making. As the EC study on due diligence requirements through supply chains shows, only 37 per cent of business respondents undertake due diligence accounting for all human rights and environmental impacts, and 16 per cent cover the entire value chain.

Even when due diligence practices are established, companies do not often disclose data resulting from the steps of a due diligence process. In the 2019 WDI report on Human Rights Due Diligence, only 30 per cent of companies reported whether they had identified any risks to worker's rights in their tier one supply chains, even to report that none were identified.

A legal framework for environmental and human rights due diligence must be established at the EU level to ensure that the same rules apply to all companies in Europe. An EU-wide legislation applicable to all business enterprises domiciled or based in the EU, or active on the EU market, will help prevent and mitigate human rights abuses and environmental harms while ensuring a level playing field and a coherent legal framework within the EU. This should create the much needed accountability for the harms to people and the planet in order to drive positive systemic changes around the world.

Question 3: If you think that an EU legal framework should be developed, please indicate which among the following possible benefits of an EU due diligence duty is important for you (tick the box/multiple choice)?
☐**Ensuring that the company is aware of its adverse human rights, social and environmental impacts and risks related to human rights violations other social issues and the environment and that it is in a better position to mitigate these risks and impacts**
☐**Contribute effectively to a more sustainable development, including in non-EU countries**
☐**Levelling the playing field, avoiding that some companies freeride on the efforts of others**
☐**Increasing legal certainty about how companies should tackle their impacts, including in their value chain**
☐**A non-negotiable standard would help companies increase their leverage in the value chain**
☐**Harmonisation to avoid fragmentation in the EU, as emerging national laws are different**

☐**SMEs would have better chance to be part of EU supply chains**

☐**Other**

Other, please specify:

In addition to the above, an important benefit of an EU due diligence duty would be that it would enable and support remedy for victims of human rights abuses or environmental harm in and outside the EU. An EU due diligence duty requires active engagement in remediation of adverse impacts where business enterprises cause or contribute to harm by way of actions or omissions. Moreover, a due diligence legislation should allow victims, in and outside the EU, to hold enterprises civilly liable for harm before EU courts. Such legal liability provisions coupled with effective enforcement mechanisms will create an important opportunity for access to remedy for victims and affected communities.

Other potential benefits of an EU due diligence duty may include:

- allowing shareholders, investors and business partners to reflect due diligence implementation in their economic decisions;
- ensuring high quality ESG data is provided to investors by corporates, allowing investors to undertake effective monitoring and stewardship;
- the EU setting an example to other markets and regulators;
- increased power and leverage of stakeholders throughout the value chain.

Question 3a. Drawbacks

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

☐**Increased administrative costs and procedural burden**

☐**Penalisation of smaller companies with fewer resources**

☐**Competitive disadvantage vis-à-vis third country companies not subject to a similar duty**

☐**Responsibility for damages that the EU company cannot control**

☐**Decreased attention to core corporate activities which might lead to increased turnover of employees and negative stock performance**

☐**Difficulty for buyers to find suitable suppliers which may cause lock-in effects (e.g. exclusivity period/no shop clause) and have also negative impact on business performance of suppliers**

☐**Disengagement from risk markets, which might be detrimental for local economies**

☐**Other**

Other, please specify:

Regarding the alleged risk of penalisation of smaller companies with fewer resources, it is worth noting that, as stressed by international standards on corporate due diligence, the means through which SMEs will be expected to meet their responsibility to respect human rights and the environment would be proportional to, among other factors, their size. Moreover, the Commission's study on due diligence requirements through the supply chain shows that, even for SMEs, the costs of carrying out mandatory supply chain due diligence appears to be relatively low compared to the company's revenue. Risk management is not less important for SMEs than for large public companies, although the form it takes may be different.

With regard to the alleged risk of decreased attention to core corporate activities which might lead to increased turnover of employees and negative stock performance, available evidence indicates otherwise. In particular, the OECD study "Quantifying the Costs, Benefits and Risks of Due Diligence for Responsible Business Conduct" (June 2016), which analysed the compliance cost of a variety of due diligence mechanisms and the economic benefits for businesses of responsible business conduct including corporate due diligence, found that comprehensive due diligence correlates to many positive key findings, including, in terms of stock performance: outperformance in stock price, increased shareholder returns, reduced volatility, improved investor satisfaction; and, in terms of human resources: increased ability to attract and retain talent, reduced turnover, recruitment and training costs, and improved reputation.

Regarding the alleged risk of disengagement from risky markets, which might be detrimental for local economies, it is worth stressing that as per international due diligence standards, disengagement should only be considered as a last resort after all other steps have been exhausted, as outlined in UN Guiding Principle 19, which notes that business enterprises should only consider ceasing relationships where options for leverage to prevent or mitigate negative impacts have been exhausted or leverage is insufficient.

A potential drawback (if not explicitly addressed in the legislation) is the risk that, if poorly implemented, parent and lead companies end up passing the additional costs of compliance with due diligence requirements to their suppliers and subcontractors, and ultimately to the most vulnerable parts of the value chains, without adapting their own purchasing practices. Power relations between multinational buyers/retailers and suppliers/producers in production countries are asymmetric and characterized by downward pressures on prices. Complementary action is therefore required to address these power imbalances and ensure a more equitable distribution of costs and benefits in global value chains, including by reforming corporate governance and ensuring transparency (see FTAO report on Making Human Rights Due Diligence Frameworks Work for Small Farmers and Workers, 2020).

Section II: Directors' duty of care – stakeholders' interests

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

	Relevant	Not relevant	I do not know/I do not take position
the interests of shareholders	X	☐	☐
the interests of employees	X	☐	☐
the interests of employees in the company's supply chain	X	☐	☐
the interests of customers	X	☐	☐
the interests of persons and communities affected by the operations of the company	X	☐	☐
the interests of persons and communities affected by the company's supply chain	X	☐	☐
the interests of local and global natural environment, including climate	X	☐	☐
the likely consequences of any decision in the long term (beyond 3-5 years)	X	☐	☐
the interests of society, please specify	X	☐	☐
other interests, please specify	X	☐	☐

the interests of society, please specify:

We support the introduction of a requirement for corporate directors to integrate wider societal interests, in line with Action 10 (ii) of the Sustainable Finance Action Plan on the "possible need to clarify the rules according to which directors are expected to act in the company's long-term interest". The Commission study on directors' duties and sustainable corporate governance once again shows a pervasive short-term tendency among listed companies within the EU, highlighting a clear upward trend in corporate pay-outs to shareholders compared to revenues vis-à-vis a declining ratio of investment to revenues. Hence, alongside explicitly integrating sustainability issues into investor duties, a successful transition towards an economy with business models and corporate behaviour that limit impacts on the environment and communities also requires an adequate EU regulatory framework on company law and corporate governance.

Resilient and successful companies need to be aware of the context in which they conduct business. Companies and markets in general thrive in prosperous and cohesive societies. There are numerous societal interests that have a profound effect on the company and the risks it is facing, including climate change, loss of biodiversity, social conflict, discrimination, corruption, poverty and human rights abuses. As was also described in the King IV report of South Africa, companies need to consider the triple context of economy, society and environment, and their governing bodies need to take account of the legitimate and reasonable needs, interests and expectations of all material stakeholders the execution of their duties in the best interests of the organization over time. However, it would be impossible and ineffective to enumerate all the types of interests that companies' directors need to take into consideration. Issues of concern depend on the business, societal and environmental context in which the company operates.

Other interests, please specify:

<u>The interest of suppliers:</u> Power imbalances exist between suppliers and companies, just as they do between companies and workers. The pandemic has highlighted that for some products, risks are being passed on down the supply chain. In the garment sector for instance, sudden cancellations of buyers' orders were common at the onset of the crisis, resulting in widespread worker lay-offs and dismissals in production countries. Some suppliers reported that they were not in a position to push back against changes to contract terms and buyer policies because of the potential impacts on their reputation, relationships and viability. [1] Currently, it is not obvious that suppliers' interests are being considered in decision making.

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

	I strongly agree	I agree to some extent	I disagree to some extent	I strongly disagree	I do not know	I do not take position
Identification of the company´s stakeholders and their interests	X	☐	☐	☐	☐	☐
Management of the risks for the company in relation to	X	☐	☐	☐	☐	☐

[1] https://www.ilo.org/wcmsp5/groups/public/---asia/---ro-bangkok/documents/briefingnote/wcms_758626.pdf

stakeholders and their interests, including on the long run						
Identification of the opportunities arising from promoting stakeholders' interests	☐	☐	☐	☐	☐	X

Please explain:

In principle, the duty of care that directors owe to the company already requires them to address the abovementioned points. However, in practice, this is not leading to proper corporate identification and due consideration of impacts on people and the planet and related risk management. Therefore, the clarification that directors should, as part of their duties, duly consider such impacts is a necessary first step in addressing this gap in practice. Challenges include the continued focus on maximising financial returns rather than considering beneficiaries' wider non-financial interests, and an over-focus on financial materiality at the expense of social and environmental materiality. The strong pressures from outside company law, the lack of meaningful reporting on sustainability metrics and the general lack of clarity on how to appropriately address stakeholders' interests mean that the problem of short-termism cannot be solved simply by requiring or permitting directors to have regard to sustainability and the company's long-term interest.

To ensure that this aspect of their duty of care is implemented by corporate boards, the law must clarify how the stakeholders' interests should be considered, both from the perspective of respect to legitimate interests of stakeholders, as well as from the perspective of the management of risks and opportunities.
This can be achieved by specifying directors' responsibilities with respect to:

- overseeing and ensuring the quality of the materiality determination (as specified in the EU Non-Financial Reporting Framework, and with due respect to the principle of double materiality) and due diligence processes (which should ideally be specified in the EU due diligence legislation); and
- determining company's strategy to address the risks and impacts identified by these processes, that is, including:
- material environmental and social risks and impacts to the company's business model, operations and supply chain.
- severe actual and potential impacts to people and the planet identified by the company's environmental and human rights due diligence in accordance with its legal obligations.
- internal measures to align firms' equity with the requirements and objectives of such sustainability strategy, targets (see question 7) and related investments. In particular, sufficient reserves should be constituted through adequate retained earnings, allocated to a dedicated reserve account, to match future investments needs for the climate transition and employee or supply chain related matters.

This approach would provide clear guidance to directors on how to properly consider stakeholders interests from the perspective of the best interest of the company, which they are already expected to do in the framework of their existing duties, rather than imposing any new behavioural obligation or changes to the corporate governance system.

The purpose of such clarification is to ensure that the sustainability matters are duly considered at a strategic level, and that there is a transparency concerning their integration in the company's overall strategy that facilitates meaningful engagement of investors and stakeholders, which includes publishing an annual overview of the stakeholders to which the company should have regard and the steps they have taken to ensure those interests have been taken into account.

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

☐I strongly agree

☐I agree to some extent

☐I disagree to some extent

☐I strongly disagree

☐I do not know

☐I do not take position

Please explain:

The upcoming initiative should consider how boards can address impacts and risks on a regular basis, supported by relevant committees (sustainability, audit, risk, remuneration), as well as the need for relevant expertise within and outside the board, thanks to ad hoc nominations of external board advisers or non-executive board members, regular updates from relevant senior management and training for board members and company executives.

Most importantly, the boards should be responsible for overseeing and ensuring the quality of the materiality determination and due diligence processes. To support the implementation of this duty, a non-executive committee, composed of independent experts and key managers of the company and chaired by a designated non-executive director, should be set up and tasked with monitoring and reviewing the content and implementation of the sustainability strategy.

As part of their duty of care, directors should be required to integrate sustainability matters into corporate strategy and their business model where necessary, and to make sufficient resources available to management. As part of this integration, directors should be required to develop, disclose and implement, on behalf of the company, a forward-looking sustainability strategy and set measurable, specific, verifiable, time-bound targets, plans and milestones to achieve them. These should be based, where appropriate, on a science-based methodology that effectively addresses:

- material environmental and social risks and impacts to the company’s business model, operations and supply chain, and
- severe impacts to people and the planet identified by the company’s environmental and human rights due diligence, including through stakeholder engagement, with a focus on workers, affected communities, in accordance with its legal obligations.

Whenever applicable, those targets need to be aligned with the EU’s and Member States’ international commitments, such as the Paris Agreement and UN Sustainable Development Goals.
Measurable targets for the mitigation of such risks and impacts are critical from several perspectives:

- Targets and KPIs are indispensable for the management of risks and impacts. If the risks or impacts meet the threshold of materiality or severity, they ought to be managed.
- The board must set such targets, in particular where effective management of risks and impacts have implications for the company's overall strategy, business model and financial planning. That means that the bigger risks and impacts are, the greater the need is for board-level decisions on strategies and targets.

- The targets are necessary to ensure transparency concerning the effectiveness of the company's management of the identified risks and impacts, and as such they are critical for engagement by investors and other stakeholders. This further requires that the company sets and reports not only on overarching targets (such as an ambition to meet the Paris Agreement goals), but also on transition plans and milestones (intermediary targets) to reach such overarching targets, to enable interested stakeholders to understand whether and how companies are progressing towards those targets.

Different departments should not be given targets that are at odds with the implementation of mitigation or prevention measures as a response to identified risks. For example, purchasing teams should not be mandated to only source the cheapest products or have unreachable margin targets, as it will go against the objective of sourcing sustainable products that are produced in respect of human rights and the environment.

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

☐I strongly agree

☐I agree to some extent

☐I disagree to some extent

☐I strongly disagree

☐I do not know

☐I do not take position

Please provide an explanation or comment:

The directors' duty of care is owed to the company. Therefore, in principle, it already includes an obligation for directors to consider all matters and stakeholders' interests. Where directors pursue the goal of maximising short-term shareholder value, it is a product not of legal obligation, but of the pressures imposed on them by financial markets, activist shareholders, the threat of hostile takeover and/or stock-based compensation schemes. These strong pressures from outside company law mean the problem of short-termism cannot be solved simply by requiring or permitting directors to have regard to sustainability and the long-term interests of the company. The interests of the providers of capital should not unduly prioritised.

A further problem is that while short-term financial performance is expressed in clear numbers, the interests of other stakeholders and their effects on the company cannot always be expressed in a similar quantifiable manner. In other words, these potentially conflicting interests are of a different fundamental quality, and therefore they cannot be simply balanced.

It is useful to confirm that the duty of care means that all legitimate interests and needs must be taken into account, and the interests of the providers of financial capital should not be unduly prioritised. However, to give it a practical effect, the law should provide a clear minimum threshold for respecting legitimate interests of stakeholders. In this regard, the directors' duty of care should provide that directors should ensure that the company:

- implements a robust due diligence to identify and address severe impacts to people and the planet linked to the company's business model;
- puts in a place a strategy and clear targets to effectively address the identified impacts in accordance with the company's legal obligations.

Failure to implement the strategy should be considered a breach of executive directors' duty of good faith (where deliberate) or duty of care (where accidental) and could be enforced by the shareholders by derivative action where the failure causes long-term harm to the company. Non-executive directors should have a duty of care to monitor the implementation of the strategy. A national regulatory body should be empowered to bring proceedings against the executive directors where non-implementation has caused serious harm or unlawful harm to third parties or the environment.

Question 9. Which risks do you see, if any, should the directors' duty of care be spelled out in law as described in question 8?

If the European Commission decides to implement such changes to the duty of care, we would strongly advise the Commission to first carry out an evaluation of the impact of similar reforms in Brazil, India and the UK.

How could these possible risks be mitigated? Please explain.

Instead of a broad mandate to balance the interests of stakeholders, the legal definition of duty of care should:

- confirm that its primary objective is to ensure long-term success of the company, taking into account its impact on people and the environment, and that in doing so directors must take into consideration all legitimate stakeholders' interests and needs, instead of prioritising the interests of providers of financial capital; and

- specify that it is an obligation of directors to ensure the implementation by the company of a robust due diligence process to identify and address severe impacts to people and the planet linked to the company's business model; and to put in a place a strategy supported by targets to address such impacts in accordance with the company's legal obligations.

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

There is a growing movement of investors that are highly supportive of companies' engagement with stakeholders' interests, the purpose of business, as well as of stronger public policies in this regard. This includes for example the UN Principles for Responsible Investment, or the Investors Alliance for Human Rights, the Workforce Disclosure Initiative signatories, as well as, broadly speaking the Sustainable Investors Forum(s).

Effective stewardship is widely regarded as a driver of enhanced operational and financial performance. It helps to reduce risks and maximise returns at the individual investment level, as well as enhance overall market stability and maximise positive impacts on society and the environment more generally.

Shareholder resolutions are an essential aspect of stewardship. They demonstrate clear asks and investor expectations to companies. Climate-related shareholder resolutions were filed at Barclays (2020) and HSBC (2021) that were each supported by over 100 institutional and private investors. The Barclays resolution was supported by 24% of all investors in the company.

A lot remains to be done, however, to improve investors' stewardship of companies. In a recent ShareAction report, the voting behaviour of 60 of the world's largest asset managers on 102 shareholder resolutions on climate change, climate-related lobbying, and social issues was analysed. It concluded that one in six asset managers did not use their voting rights at over 10 per cent of the resolutions they could have voted on. Whilst European asset managers have better voting performance, they do not tend to file shareholder resolutions on climate change and social issues in their own jurisdictions. Only two social resolutions were filed in Europe in 2020 (at H&M and Novo Nordisk), however both received less than five per cent support. Only six out of the 53 climate resolutions covered in this analysis were filed in Europe. Practically, it is more complex and difficult to file a shareholder resolution in most European markets compared to the US, due to additional legal and regulatory hurdles, including higher ownership requirements. Changes to legislation in this area would make it easier for shareholders to demonstrate their support for stakeholder concerns about companies.

Question 10. As companies often do not have a strategic orientation on sustainability risks, impacts and opportunities, as referred to in question 6 and 7, do you believe that such considerations should be integrated into the company's strategy, decisions and oversight within the company?

☐**<u>I strongly agree</u>**

☐**I agree to some extent**

☐**I disagree to some extent**

☐**I strongly disagree**

☐**I do not know**

☐**I do not take position**

Please explain:

Addressing sustainability challenges often requires changes to the company's business model, strategy and financial planning. Therefore, it is critical that the company's strategy and targets with respect to such risks, impacts and opportunities is considered as part of the overall corporate strategy and is decided on and monitored by the governing body of the company. Some companies already implement such an approach.

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

Please describe examples:

In all EU Member States, directors' duty of care is owed primarily to the company. A derivative action presented by the shareholders of a company on the company's behalf may be brought where the company suffers loss as a result of a breach in the directors' duty of care. In this case, shareholders can initiate litigation to enforce directors' duty of care on behalf of the company. However, derivative actions are rare in Europe and the enforcement levels of directors' duties are low in all Member States[2]

All cases to date seeking remedies for stakeholders have been against companies as a legal entity and not directors. There is some existing tort law, such as under the Italian civil code, which could enable a stakeholder to bring a claim against a director for a breach of directors' duty, but the degree of proof needed, and causation shown makes the success of such claims difficult.

Question 12. What was the effect of such enforcement rights/actions? Did it give rise to case law/ was it followed by other cases? If not, why?
Please describe:

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

☐**I strongly agree**

☐**<u>I agree to some extent</u>**

☐**I disagree to some extent**

☐**I strongly disagree**

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[2] IFC (2015). A Guide to Corporate Governance Practices in the European Union, pg.50-53. https://www.ifc.org/wps/wcm/connect/506d49a2-3763-4fe4-a783-5d58e37b8906/CG_Practices_in_EU_Guide.pdf?MOD=AJPERES&CVID=kNmxTtG.

☐**I do not know**
☐**I do not take position**

Please explain your answer:

The growing diversification and interconnectedness of the world in which companies operate means that if they are to navigate growing systemic uncertainty, directors must understand the purpose and impact of the company they lead, and to do this they must listen to stakeholders affected by the activities of the company. If stakeholders believe that directors are not considering their interests which are relevant for the long-term sustainability of the company, resulting in a breach of directors' duty of care, stakeholders should have the opportunity and means to enforce directors' duty of care.

The definition of stakeholders involved in the enforcement of directors' duty of care depends on the company and the context in which operates; however, it should at least include the following:

- **workers:** workers of all types should be regarded as stakeholders including those in traditional forms of employment, along-side self-employed workers in the gig economy, those employed through third parties, those working as contractors and as seasonal workers, and those in supply chains. Trade unions and similar bodies provide a democratic means for workers to speak collectively and should also be regarded as stakeholders involved in the enforcement of the duty of care.
- **suppliers:** as power imbalances exist between suppliers and companies, they should be regarded as stakeholders involved in the enforcement of the duty of care.
- **communities directly affected by corporate activity:** communities should be regarded as stakeholders able to enforce directors' duty of care in the AGM process, and include:
  - those affected in a local, geographical sense by corporate operations.
  - those affected in a global sense by corporate operations and activity on the climate crisis.
  - communities who have been historically been, and continue to be, oppressed because of a company's actions, including but not limited to the LGBTQIA+ community, racially oppressed people, the disabled community and women and non-binary people.
- **communities indirectly affected by corporate activity:** the complexity of the systemic challenges that companies face, and the interconnectedness of a globalised world, means that individuals and organisations can be affected by corporate activities at great geographical and temporal distance. Those who are indirectly severely affect by company activities should be regarded as stakeholders.
- **customers and users:** consumers associations are one way that customers come together, and they should be regarded as stakeholders involved in the enforcement of the duty of care. In order to reflect the growth in business practices product users should also be regarded as stakeholders, as they are significantly affected by what a company does.

However, the enforcement of directors' duty of care by stakeholders does not refer to the initiation of legal action against directors or the granting of voting rights. Directors should continue to be legally held accountable to shareholders only, and therefore shareholders should be the only party permitted to initiate litigation to enforce directors' duty of care. Instead, stakeholders should play a role in the enforcement of directors' duty of care through three avenues in the corporate activities of a company, as explained in detail below.

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

The current Annual General Meeting (AGM) of a company is the only regular company forum where companies, shareholders and stakeholders can come together to meet and exchange views. We hold the view that companies and directors' boards, through AGMs, should create a purposeful ongoing process through which they will gather insight from stakeholders, providing three avenues in which stakeholders can enforce directors' duty of care:[3]

- **process of engagement with stakeholder groups throughout the year:**
  - a value-based purpose for AGMs will empower stakeholders to speak up and share their experiences, including concerns on a breach of directors' duty of care.
  - to do this, stakeholders will have the right to meet in person or by video call and have a substantive discussion with the company at least once, discussing overlapping areas of concerns, such as a breach of directors' duty of care.
  - these meetings will be led by a chair and have at least one board member present, giving stakeholders the right to address a breach of directors' duty of care to directors directly.
  - following the publishing of the annual report, stakeholders will be invited to submit a question via the company email which could include questions of potential concerns on directors' duty of care. The company will publish all questions, as well as their responses to them, on their website in advance of the AGM, ensuring accountability when stakeholder questions on directors' duty of care are addressed.
- **shareholders:**
  - throughout the above process of engagement, shareholders will be able to hear, challenge and discuss the views of stakeholders impacted by corporate activity, including any issues on directors' duty of care.
  - this will better inform shareholders when holding companies and directors to account for their impacts on stakeholders.
  - the voting element of the AGM will be split from the discursive element. Currently, shareholders can vote in advance of the AGM – rendering much of the interaction there hollow. At the AGM of the future, the vote will take place after the AGM, so shareholders can gauge stakeholder views and board responses to them first. This will give shareholders the opportunity to assess and interrogate company performance regarding stakeholders concerns on directors' duty of care at the AGM in a way that informs their enforcement of director's duties of care through voting.
- **AGM event itself:** this event will be a meeting focusing on how directors' have fulfilled their responsibility to stakeholders, including their responses to allegations of breach in duty of care.
  - at the event, stakeholders will be able to meet and continue nuanced dialogue with the board of directors on any issues surrounding directors' duty of care.
  - companies will post a summary of the discussion and list of action points on the company website after the AGM event. These will be considered at the annual learning review during the AGM in the following year, permitting stakeholders concerns on directors' duty of care to be integrated into corporate decision-making and subsequently addressed.
  - the AGM should take place in a hybrid format – supporting investors and stakeholders to attend, whatever their location.

Section III: Due diligence duty

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

[3] SA (2021). Fit-for-purpose? The future of the AGM. https://shareaction.org/wp-content/uploads/2021/01/Future-of-the-AGM.pdf

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

It should be clarified that the due diligence duty's ultimate goal must be to respect human rights and the environment in a company's own operations, global value chains and within their business relationships (due diligence is the strategy mandated to achieve that goal).

Prior to ceasing, preventing, mitigating and accounting for human rights, health and environmental impacts, companies should first be obliged to effectively identify and assess any actual or potential adverse human rights and environmental impacts with which they may cause, contribute to or be directly linked to, both through their own activities and as a result of their business relationships.

Companies should also track and monitor the implementation and effectiveness of the adopted measures. This includes the collection of relevant data specific to the risk(s), such as data disaggregated by supplier and gender. The results of these tracking and monitoring processes must be used to inform possible changes to the global business operations and human rights and environmental due diligence process

.

We agree due diligence must be a risk based and proportionate approach. Companies should thus map out their global value chain, the human rights and environmental risks at each level of their value chain and prioritise their due diligence processes depending on the risks. Companies should take proportionate and commensurate measures based on the severity of the risks and the specific circumstances, particularly their sector of activity, the size and length of their supply chain, and the size of the undertaking.

Moreover, the "due diligence duty" should cover the company's' global value chain, which includes entities with which it has a direct or indirect business relationship (understood as all types of business relationships of the enterprise – suppliers, franchisees, licensees, joint ventures, investors, clients, contractors, customers, consultants, financial, legal and other advisers, and any other non-State or State entities linked to its business operations, products or services; as per the OECD Due Diligence Guidance for Responsible Business Conduct, p.10) and which either (a) supply products or services that contribute to the company's own products or services, or (b) receive products or services from the company. Supply chains and value chains are similar terms that refer to the entire production chain. However, while "supply chain" may be used to specifically refer to the production and distribution of a commodity, "value chain" includes the set of interrelated activities by which a company adds value to an article. At the end of the definition, it could be clarified that, in all instances, due diligence is a continuous and gradual process and companies should exercise their leverage and meaningfully engage with their suppliers and business partners to support them in improving their practices.

Lastly, while not strictly part of the definition, it could be clarified that due diligence must enable and support the provision of remedy. The obligation to respect human rights and the environment requires active engagement in the remediation of adverse impacts where companies cause or contribute to harm by way of actions or omissions, or, where a company has not caused or contributed to the harm but its operations, products or services are directly linked to it, the obligation to exercise or increase its leverage over those responsible to help ensure that remediation is provided.

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

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

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

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

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

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

☐**None of the above, please specify**

Please specify:

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

Question 15b: **Please provide explanations as regards your preferred option, including whether it would bring the necessary legal certainty and whether complementary guidance would also be necessary.**

Option 3 is our preferred option as this would create legal certainty and a level playing field for companies as to the necessary processes to be put in place and impacts to be covered by the due diligence duty. A rich body of legally binding international human rights and labour standards has long been developed, leaving no room for legal uncertainties. Although not as straight-forward as human rights standards, environmental standards - often addressed to states - can also be translated into concrete obligations for companies.

It is important that the legislation include further requirements for environmental issues. The definition should follow a model covering all environmental impacts and containing references to specific environmental issues (e.g. climate change, air, soil and water pollution, loss of biodiversity) and legal instruments. EU law should specify the expected standard of business conduct in this regard. This would guide companies when they conduct due diligence, and administrative and judicial authorities when determining liability. Existing international due diligence standards already constitute a useful reference in this regard.

The requirements should be applicable to all sectors, including the financial industry. The financial sector comprises a wide range of businesses and activities, from asset owners and managers to private equity, venture capital and commercial banking. Each of these actors have their own characteristics and therefore different potential human rights and environmental risks in their business relationships. Nevertheless, for all financial institutions alike, failing to examine social and environmental records can result in the facilitation of human rights violations and environmental damage. Mandatory environmental and human rights due diligence can help ensure companies, including financial institutions, address their human rights and environmental risks. In addition, such legislation prevents companies, including in the financial sector, that disregard the impacts of their activities on the environment and human rights, from undercutting others that are more adequately assessing and mitigating these risks. It is thus essential that the scope of the forthcoming due diligence initiative covers all financial institutions.

Financial institutions, like other companies, should avoid causing or contributing to adverse impacts and seek to prevent or mitigate those impacts when their operations, products and services can be directly linked to them through a business relationship. Research shows that many financial institutions do not sufficiently take environmental and social factors into consideration. In 2020, ShareAction[4] assessed the approaches of 75 asset managers to human and labour rights. That assessment concluded that a majority of asset managers only conduct basic reactive engagement where human rights abuses have already occurred, in order to minimise financial risk to the portfolio, as opposed to proactively engaging to strengthen due diligence and reporting on salient human rights issues.

Currently, certain EU due diligence requirements already apply to financial institutions, but many gaps remain. The Non-Financial Reporting Directive for instance requires banks and insurers with more than 500 employees to report on non-financial issues, on a 'comply or explain' basis. The Sustainable Finance Disclosure Regulation includes certain due diligence requirements but those are limited to entity level or only apply to certain products, and only the largest firms (500 staff or more) must disclosure "principle adverse impacts" or negative ESG impacts of their investments. On these grounds, it is all the more necessary that the forthcoming legislation introduces due diligence processes binding both companies and financial institutions.

The power and influence of the financial sector is widely recognised. It is therefore of utmost importance that all financial institutions are explicitly included in the scope of the due diligence obligations. Moreover, this will provide greater clarity in the industry as well as create a level playing field.

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

☐**Human rights, including fundamental labour rights and working conditions (such as occupational health and safety, decent wages and working hours)**

☐**Interests of local communities, indigenous peoples' rights, and rights of vulnerable groups**

☐**Climate change mitigation**

☐**Natural capital, including biodiversity loss; land degradation; ecosystems degradation, air, soil and water pollution (including through disposal of chemicals); efficient use of resources and raw materials; hazardous substances and waste**

☐**Other, please specify**

Other, please specify:

The material scope of the EU directive should cover all human rights, including workers' and trade union rights; social, health and environmental standards; as well as good governance international standards.

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

N/A

[4] https://shareaction.org/the-worlds-largest-asset-managers-pay-lip-service-to-preventing-human-rights-abuse/

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

The effectiveness of the due diligence duty will very much depend on the robustness of the criteria and 'performance standards' against which the due diligence should be conducted.

Regarding human and labour rights, due diligence legislation should at least cover all internationally recognized standards, understood, at a minimum, as those expressed in:

- the International Bill of Human Rights,
- Customary international law,
- International Humanitarian Law,
- international human rights instruments on the rights of persons belonging to particularly vulnerable groups or communities (including the International Convention on the Elimination of All Forms of Racial Discrimination, the Convention on the Elimination of All Forms of Discrimination against Women, the Convention on the Rights of the Child, the International Convention on the Protection of the Rights of All Migrant Workers and Members of their Families, the Convention on the Rights of Persons with Disabilities, the United Nations Declaration on the Rights of Indigenous Peoples, the Declaration on the Rights of Persons Belonging to National or Ethnic, Religious and Linguistic Minorities) and
- the principles concerning fundamental rights set out in the ILO Declaration on Fundamental Principles and Rights at Work, as well as those recognised in the ILO Convention on freedom of association and the effective recognition of the right to collective bargaining, the ILO Convention on forced labour, the ILO Convention on the abolition of forced labour, the ILO Convention on the worst forms of child labour, the ILO Convention on the elimination of discrimination in respect of employment and occupation and ILO Convention on equal remuneration; and other rights recognised in a number of ILO Conventions, such as freedom of association, minimum age, occupational safety and health, living wages, indigenous and tribal peoples' free and informed consent (ILO Convention on indigenous and tribal peoples),
- the rights recognised in the African Charter of Human and Peoples' Rights, the American Convention on Human Rights, the European Convention on Human Rights, the European Social Charter, the Charter of Fundamental Rights of the European Union, and
- national constitutions and laws recognising or implementing human rights.

Question 15f: If you ticked option 4) in question 15, which sectors do you think the EU should focus on?
N/A

Question 15g: If you ticked option 5) in question 15, which themes do you think the EU should focus on?
N/A

Question 16: How could companies'- in particular smaller ones'- burden be reduced with respect to due diligence? Please indicate the most effective options (tick the box, multiple choice possible)
This question is being asked in addition to question 48 of the Consultation on the Renewed Sustainable Finance Strategy, the answers to which the Commission is currently analysing.

☐All SMEs should be excluded

☐SMEs should be excluded with some exceptions (e.g. most risky sectors or other)

☐Micro and small sized enterprises (less than 50 people employed) should be excluded

☐Micro-enterprises (less than 10 people employed) should be excluded

☐SMEs should be subject to lighter requirements (“principles-based” or “minimum process and definitions” approaches as indicated in Question 15)

☐SMEs should have lighter reporting requirements

☐Capacity building support, including funding

☐Detailed non-binding guidelines catering for the needs of SMEs in particular

☐Toolbox/dedicated helpdesk for companies to translate due diligence criteria into business practices

☐Other option, please specify

☐None of these options could be pursued

Please explain your choice, if necessary:

From international standards (UN Guiding Principles on Business & Human Rights, OECD Guidelines for Multinational Enterprises), it is very clear that due diligence is the obligation of all companies. All business enterprises, regardless of size, should conduct human rights and environmental due diligence. SMEs, too, can cause, contribute to and be directly linked to severe human rights and environmental impacts. While their operations are smaller, SMEs also have a direct responsibility to respect human rights and the environment.

However, as stressed by the aforementioned international standards, the means through which companies will be expected to meet their responsibility to respect human rights and the environment should be commensurate to the severity of the risks. For SMEs, the type of policies and processes expected would be according to their capacity, following the Commentary to Principle 14 of the UN Guiding Principles on Business & Human Rights. Their degree of leverage over their business relationships should also be considered in determining their responsibility.

Studies of the compliance costs of a variety of due diligence regimes do not identify a disproportionate economic burden for SMEs. Rather the cost of compliance is typically related to the size of the enterprise. Moreover, the Commission’s study on due diligence requirements through the supply chain shows that, even for SMEs, the costs of carrying out mandatory supply chain due diligence appears to be relatively low compared to the company’s revenue. The additional recurrent company-level costs, as percentages of companies’ revenues, amount to less than 0.14% for SMEs.

SMEs do not tend to generate and encounter as many risks to human rights and the environment as larger businesses do, by virtue of the fact that their value chains are smaller. SMEs tend to have fewer suppliers and customers, which enables deeper and better-quality relationships. For this reason, not only is it often more feasible for SMEs to map the businesses in their supply chains, it is also easier and more desirable to get to know them. SMEs also tend to spend more time selecting business partners that share their values and match their standards and have a preference for longer-term relationships. These stronger relationships allow greater scope to integrate human rights and environmental issues.

Increasingly, empirical evidence is revealing that companies with responsible business conduct policies and practices, such as due diligence, are more resilient, stronger and better performing businesses. Companies that know their supply chains and actively identify and mitigate their risks generally perform better overall. Therefore, while capacity building support, including funding, could be considered as a way to foster compliance with due diligence standards, it is incorrect to only conceptualise due diligence as a burden on companies, as the evidence reveals its potential as a beneficial and valuable standard of conduct.

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

☐Yes

☐No

☐I do not know

Question 17a: What link should be required to make these companies subject to those obligations and how (e.g. what activities should be in the EU, could it be linked to certain turnover generated in the EU, other)? Please specify:
The obligation should apply to companies operating in the internal market (selling products or services, conducting activities). The link could therefore be the presence on the internal market of products or services.

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

These companies must also be obliged to respect human rights and the environment, in their own operations, subsidiaries, business relationships and global value chains, and to undertake human rights due diligence for the products, services and activities that are placed or undertaken in the EU internal market.

These companies must also be liable for any human rights abuses and environmental harm in their operations or value chains (without prejudice to other subcontracting and supply chain liability frameworks).
Governments must set up robust enforcement mechanisms, with effective sanctions, to ensure that these companies also obey the law.

Question 18: Should the EU due diligence duty be accompanied by other measures to foster more level playing field between EU and third country companies?
☐**Yes**
☐No
☐I do not know
Please explain:

Question 19: Enforcement of the due diligence duty
Question 19a: If a mandatory due diligence duty is to be introduced, it should be accompanied by an enforcement mechanism to make it effective. In your view, which of the following mechanisms would be the most appropriate one(s) to enforce the possible obligation (tick the box, multiple choice)?
☐**<u>Judicial enforcement with liability and compensation in case of harm caused by not fulfilling the due diligence obligations</u>**
☐**<u>Supervision by competent national authorities based on complaints (and/or reporting, where relevant) about non-compliance with setting up and implementing due diligence measures, etc. with effective sanctions (such as for example fines)</u>**
☐**<u>Supervision by competent national authorities (option 2) with a mechanism of EU cooperation/coordination to ensure consistency throughout the EU</u>**
☐**Other, please specify**
Please provide explanation:
We believe that all three mechanisms are necessary:
Legal liability is needed at least for human rights and environmental harms that a business enterprise, or any company that they control or have the ability to control has caused or contributed to. 'Control' should be determined according to the factual circumstances. It may also result through the exercise of power in a business relationship. It may include a situation of economic dependence. Equally, grounds for liability must be established on the basis of failure to carry out adequate due diligence.

Judicial enforcement of due diligence standards and adjudication following allegations of harm is essential for holding companies accountable and ensuring that victims have access to an effective remedy for these harms. Due diligence legislation should give effect to the internationally recognised right to effective remedy. To ensure that victims have meaningful access to remedy, the burden of proof should be reversed in proceedings against business enterprises. The limitation period for bringing legal actions must also be adapted to be reasonable and sufficient, taking into account the particularities of transnational litigation.

As a complement to judicial enforcement mechanism, competent national authorities (CAs) should be established in Member States. CAs should be empowered to perform a dual function of monitoring disclosure and due diligence performance, and initiating investigations (both on their own initiative and on the basis of complaints by third parties) where there is reason to believe that a company has breached its due diligence obligations. Breaches should give rise to administrative liability and CAs should be empowered to impose proportionate and dissuasive sanctions in such cases (infringements shall be subject to administrative fines at least up to 4% of the total worldwide annual turnover of the preceding financial year, as provided for data protection infringements in the GDPR). However, administrative liability, while a necessary complement, in no way substitutes for civil and criminal liability mechanisms. CAs should be independent from government ministries, particularly those that promote business interests in order to ensure their impartiality and prevent conflicts of interest. CAs must also be adequately resourced through financial support and staff with appropriate training and expertise.

The legislation should also establish an EU-level body with monitoring, advisory, capacity-building and standard-setting functions. This body should monitor CAs performance to ensure consistent, robust practices across Member States. It should also support the greater harmonization of approaches, including through the development of standards and guidance for CAs to help them in their evaluation and investigation tasks, and of guidance for companies to conduct due diligence. Any monitoring bodies established - judicial and non-judicial - should have clear mechanisms for stakeholders' involvement.

Finally, to safeguard opportunities for access to remedy for victims, any new enforcement and liability measures should be introduced without prejudice to other liability regimes which impose stricter or alternative grounds of liability.

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

☐Yes

☐No

In case you answered yes, please indicate what type of difficulties you have encountered or have information about:

N/A

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

N/A

Section IV: Other elements of sustainable corporate governance

Question 20: Stakeholder engagement

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

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

☐**<u>I strongly agree</u>**
☐**I agree to some extent**
☐**I disagree to some extent**
☐**I strongly disagree**
☐**I do not know**
☐**I do not take position**

Please explain:
Meaningful stakeholder engagement must be integral to the development and implementation of:

- corporate strategies;
- corporate due diligence processes, across all stages of due diligence including identification and assessment of human rights risks, as well as determination of the appropriate actions and the monitoring and evaluation of their effectiveness, reflecting the ongoing and continuous nature of human rights and environmental due diligence; and
- adequate systems for enabling access to remedy, providing remedy and compensating for loss and damages.

EU regulation requiring directors to engage with stakeholders should provide clear guidance on how mechanisms of engagement should be established and implemented to prevent abuse of power by companies. Stakeholder engagement allows businesses to understand perspectives of those who may be affected by their decisions and operations. The process of corporate strategy development should create clear opportunities for stakeholder engagement. This allows businesses to incorporate concerns and input from affected stakeholders into strategic planning and to improve performance on broader sustainability objectives. In some sectors, stakeholder engagement may need to take place at project-level.

Stakeholder engagement is critical for ensuring effective due diligence. Companies should engage affected stakeholders in the implementation of the due diligence. Specifically, companies should be required to consult affected stakeholders for the purpose of identifying and assessing human rights and environmental impacts, determining appropriate prevention, mitigation and remediation actions and evaluating their effectiveness. This could be achieved by keeping an up-to-date register of stakeholders which would give companies oversight of stakeholders affected by the due diligence process, and wider company-stakeholder relations. Effective identification of and engagement with stakeholders better prepares businesses to avoid conflicts with local communities, and provide effective remedy for harms, when required. It allows businesses to understand perspectives of those who may be affected by their decisions and activities and work towards the design of sustainable prevention and mitigation approaches.

All mechanisms for stakeholder engagement must seek to address the power imbalance between the company and the affected persons or groups and between affected groups themselves.
Engagement processes should aim to understand how existing contexts and/or vulnerabilities may create disproportionate impacts for certain groups including indigenous peoples and communities, forest communities, coastal communities, lower-caste communities and other minority groups, migrant workers, homeworkers, temporary workers, women and children, among others. Special attention should also be paid to implementing a gender-based approach to ensure the safe and equal participation of women in decision-making processes.

Where indigenous peoples and communities may be affected, businesses must be required to adhere to international standards on principles of free, prior and informed consent (FPIC). FPIC requires that indigenous peoples and communities are given the opportunity to duly consider and approve or reject projects before they begin. They should also be required to publish their internal FPIC policy.

Question 20b: If you agree, which stakeholders should be represented? Please explain.
All affected or potentially affect stakeholders, whether persons or groups, in all stages of the due diligence process - from the identification of risks to determination of appropriate actions, to monitoring and evaluating the effectiveness of the company's actions to prevent, mitigate and remedy the impacts - should be represented. This includes a range of persons and other actors who are credible proxies, such as: workers; employees' representatives; trade unions; NGOs and grassroot organisations; community members; indigenous peoples and communities; forest communities; human rights, land and environmental defenders; feminist and LGBTQ organisations, women and women's organisations; community leaders; lower-caste representatives; migrant workers and representatives; faith-based organisations; and local authorities .Relevant experts on human rights, environment, climate or other subject matter areas should form part of the stakeholder engagement process.

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

	Is best practice	Should be promoted at EU level
Advisory body	☐	☐
Stakeholder general meeting	☐	☐
Complaint mechanism as part of due diligence	☐	**X**
Other, please specify	☐	**X**

Other, please specify:

See answer to question 13a

Question 21: Remuneration of directors
Current executive remuneration schemes, in particular share-based remuneration and variable performance criteria, promote focus on short-term financial value maximisation (Study on directors' duties and sustainable corporate governance).
Please rank the following options in terms of their effectiveness to contribute to countering remuneration incentivising short-term focus in your view.
This question is being asked in addition to questions 40 and 41 of the Consultation on the Renewed Sustainable Finance Strategy the answers to which the Commission is currently analysing.
Ranking 1-7 (1: least efficient, 7: most efficient)

Restricting executive directors' ability to sell the shares they receive as pay for a certain period (e.g. requiring shares to be held for a certain period after they were granted, after a share buy-back by the company)	
Regulating the maximum percentage of share-based remuneration in the total remuneration of directors	
Regulating or limiting possible types of variable remuneration of directors (e.g. only shares but not share options)	
Making compulsory the inclusion of sustainability metrics linked, for example, to the company's sustainability targets or performance in the variable remuneration	
Mandatory proportion of variable remuneration linked to non-financial performance criteria	**6**
Requirement to include carbon emission reductions, where applicable, in the lists of sustainability factors affecting directors' variable remuneration	**6**
Taking into account workforce remuneration and related policies when setting director remuneration	**7**

Other option, please specify: Absence of remuneration criteria that directly motivate economic activity with material adverse impacts	**7**
None of these options should be pursued, please explain	

Please explain:

The abovementioned options to contribute to countering remuneration incentivizing short-term focus will have to work in tandem. It is important to not only link variable remuneration to non-financial performance but to also withhold variable remuneration that motivate economic activities with material adverse impacts (e.g. oil executives remunerated according to oil production and exploration metrics). In addition, it is key that there is clear guidance in the legislation on non-financial performance criteria.

Question 22: Enhancing sustainability expertise in the board
Current level of expertise of boards of directors does not fully support a shift towards sustainability, so action to enhance directors' competence in this area could be envisaged (Study on directors' duties and sustainable corporate governance).
Please indicate which of these options are in your view effective to achieve this objective (tick the box, multiple choice).

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

☐<u>Requirement for companies to have a certain number/percentage of directors with relevant environmental, social and or/human rights expertise</u>

☐Requirement for companies to at least one director with relevant environmental, social and/or huma rights expertise

☐<u>Requirement for the board to regularly assess its level of expertise on environmental, social and/or human rights matters and take appropriate follow-up, including regular trainings</u>

☐<u>Other option, please specify</u>

☐None of these are effective options

Please explain:

The Board should set up a non-executive committee, composed of a combination of independent experts and top managers, chaired by a designated non-executive director, and tasked with monitoring and reviewing the content and implementation of the company's sustainability strategy. The experts should have expertise relevant to the main sustainability challenges facing the company. The managers involved in the committee should include CEO and CFO. The committee should transparently report on the matters discussed, and the recommendations. The purpose of the committee would be to provide critical input for both the non-executive and executive directors' duty of care with respect to sustainability matters.

In addition, the Board, as a collective organ, should have internal expertise on sustainability matters. The number of directors and the types of the expertise should, however, be determined according to the nature and diversity of sustainability challenges facing the company, rather than the legislation. As part of their duty of care with regard to the oversight over the company's sustainability strategy and due diligence, as well as for the purpose of setting up and deciding on the composition of the sustainability committee (described above), the directors should evaluate the adequacy of their expertise.

There is also historical evidence that a lack of diversity in boards can have detrimental effects: it has been identified as a major reason for the inadequate actions of financial institutions that led to the financial crisis of 2008. Homogeneity fostered "group thinking" where risks were not identified and managed adequately by boards. Analysing root causes and regulatory failures, many actors from industry associations to trade unions identified the need for greater diversity, not just in terms of gender or race but also in terms of experience and backgrounds. This was even acknowledged in a parliamentary hearing by the Association of Financial Mutuals. In this respect, the Walker Review officially commissioned by the UK government pointed out that "the pressure for conformity on boards can be strong, generating corresponding difficulty for an individual board member who wishes to challenge group thinking". Therefore, it is important to ensure that a significant share of board members have special expertise in social, environmental and human rights matters, including feminist and anti-racist approaches, in order to achieve real impact on companies' decisions.

Over ten years have passed since the crisis but diversity on boards as not reached adequate levels, neither in terms of background nor gender nor race nor expertise, although consensus on the urgency was high both in political and corporate circles. Voluntary approaches have failed. In order to avoid repeating the mistakes of the past, policy interventions are needed, requiring firms to increase diversity on boards in terms of gender, race, background and the above-mentioned fields of expertise, developing and implementing a clear strategy how they will achieve that in an effective way.

Question 23: Share buybacks

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

☐I strongly agree

☐I agree to some extent

☐I disagree to some extent

☐I strongly disagree

☐I do not know

☐I do not take position

Question 23a: If you agree, what measure could be taken?

Question 24: Do you consider that any other measure should be taken at EU level to foster more sustainable corporate governance?

If so, please specify:

- Employees' representatives and long-term committed shareholders should be given stronger rights in the decisions concerning takeover bids.
- Gender parity on boards needs to be mandated: efforts to reform corporate governance by the European Commission cannot be dissociated from the necessity to put an end to this long-standing imbalance. Quotas introduced in France in 2011 have proven to be effective.

Section V: Impacts of possible measures

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

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

	Non-binding guidance. **Rating 0-10**	Introduction of these duties in binding law, cost and benefits linked to setting up /improving external impacts' identification and mitigation processes **Rating 0 (lowest impact)-10 (highest impact) and quantitative data**	Introduction of these duties in binding law, annual cost linked to the fulfilment of possible requirements aligned with science-based targets (such as for example climate neutrality by 2050, net zero biodiversity loss, etc.) and possible reorganisation of supply chains **Rating 0 (lowest impact)-10 (highest impact) and quantitative data**
Administrative costs including costs related to new staff required to deal with new obligations			
Litigation costs			
Other costs including potential indirect costs linked to higher prices in the supply chain, costs liked to drawbacks as explained in question 3, other than administrative and litigation costs, etc. Please specify.			
Better performance stemming from increased employee loyalty, better employee performance, resource efficiency			
Competitiveness advantages stemming from new customers, customer loyalty,			

sustainable technologies or other opportunities			
Better risk management and resilience			
Innovation and improved productivity			
Better environmental and social performance and more reliable reporting attracting investors			
Other impact, please specify			

Please explain:

Question 26: Estimation of impacts on stakeholders and the environment
A clarified duty of care and the due diligence duty would be expected to have positive impacts on stakeholders and the environment, including in the supply chain. According to your own understanding and assessment, if your company complies with such requirements or conducts due diligence already, please quantify / estimate in quantitative terms the positive or negative impact annually since the introduction of the policy, by using examples such as:

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