

# Consultation Document Proposal for an Initiative on Sustainable Corporate Governance

Fields marked with \* are mandatory.

## Disclaimer

This document is a working document of the Commission services for consultation and does not prejudice the final decision that the Commission may take.

The views reflected on this consultation paper provide an indication on the approach the Commission services may take but do not constitute a final policy position or a formal proposal by the European Commission.

Please note that in order to ensure a fair and transparent consultation process only responses received through the online questionnaire will be taken into account and included in the report summarising the responses.

## Introduction

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### Political context

The Commission's political guidelines set the ambition of Europe becoming the world's first climate-neutral continent by 2050 and foresee strong focus on delivering on the UN Sustainable Development Goals[1], which requires changing the way in which we produce and consume. Building on the political guidelines, in its Communication on the European Green Deal[2] (adopted in December 2019) and on A Strong Social Europe for Just Transition[3] (adopted in January 2020) the Commission committed to tackling climate and environmental-related challenges and set the ambition to upgrade Europe's social market economy.

The European Green Deal sets out that "sustainability should be further embedded into the corporate governance framework, as many companies still focus too much on short-term financial performance compared to their long-term development and sustainability aspects."

Sustainability in corporate governance encompasses encouraging businesses to frame decisions in terms of their environmental (including climate, biodiversity), social, human and economic impact, as well as in terms of the company's development in the longer term (beyond 3-5 years), rather than focusing on short-term gains.

As a follow-up to the European Green Deal, the Commission has announced a sustainable corporate governance initiative for 2021, and the initiative was listed among the deliverables of the Action Plan on a Circular Economy[4], the Biodiversity strategy[5] and the Farm to Fork strategy[6]. This initiative would build on the results of the analytical and consultative work carried out under Action 10 of the Commission's 2018 Action Plan on Financing Sustainable Growth and would also be part of the Renewed Sustainable Finance

Strategy.

The recent Communication “Europe's moment: Repair and Prepare for the Next Generation” (Recovery Plan)[7] (adopted in May 2020) also confirms the Commission’s intention to put forward such an initiative with the objective to “ensure environmental and social interests are fully embedded into business strategies”. This stands in the context of competitive sustainability contributing to the COVID-19 recovery and to the long-term development of companies. Relevant objectives are strengthening corporate resilience, improving predictability and management of risks, dependencies and disruptions including in the supply chains, with the ultimate aim for the EU economy to build back stronger.

This initiative is listed in the Commission Work program for 2021 [8].

EU action in the area of sustainable corporate governance will complement the objectives of the upcoming Action Plan for the implementation of the European Pillar of Social Rights, to ensure that the transitions towards climate-neutrality and digitalisation are socially sustainable. It will also strengthen the EU's voice at the global scene and would contribute to the respect of human rights, including labour rights– and corporate social responsibility criteria throughout the value chains of European companies – an objective identified in the joint Communication of the Commission and the High Representative on the Global EU response to COVID-19[9].

This initiative is complementary to the review of the Non-Financial Reporting Directive (NFRD, Directive 2014/95/EU[10]) which currently requires large public-interest companies to disclose to the public certain information on how they are affected by non-financial issues, as well as on the company’s own impacts on society and the environment. The NFRD also requires companies to report on their social and environmental policies and due diligence processes if they have them, or otherwise explain why they do not have any (comply or explain approach). Whilst the NFRD is based on incentives “to report”, the sustainable corporate governance initiative aims to introduce duties “to do”. Such concrete actions would therefore contribute to avoiding “greenwashing” and reaching the objectives of the on-going review of the NFRD too, in particular the aim of enhancing the reliability of information disclosed under the NFRD by ensuring that the reporting obligation is underpinned by adequate corporate and director duties, and the aim of mitigating systemic risks in the financial sector. Reporting to the public on the application of sustainability in corporate governance and on the fulfilment of directors’ and corporate duties would enable stakeholders to monitor compliance with these duties, thereby helping ensure that companies are accountable for how they mitigate their adverse environmental and social impacts.

The initiative would build upon relevant international standards on business and human rights and responsible business conduct, such as the United Nations’ Guiding Principles on Businesses and Human Rights and the OECD Guidelines for Multinational Enterprises and its Due Diligence Guidance for Responsible Business Conduct.

As regards environmental harm linked to deforestation, the Commission is also conducting a fitness check of the EU Timber Regulation and an impact assessment.

Finally, Covid-19 has put small and medium sized companies under financial pressure, partly due to increased delay in the payments from their larger clients. This raises the importance of the role of board members of companies to duly take into account the interests of employees, including those in the supply chains as well as the interests of persons and suppliers affected by their operations. Further support

measures for SMEs also require careful consideration.

## **Results of two studies conducted for the Commission**

To integrate properly sustainability within corporate strategies and decisions, the High-Level Expert Group on Sustainable Finance<sup>[11]</sup> recommended in 2018 that the EU clarifies corporate board members' duties so that stakeholder interests are properly considered. Furthermore, they recommended for the EU to require that directors adopt a sustainability strategy with proper targets, have sufficient expertise in sustainability, and to improve regulation on remuneration.

In its 2018 Action Plan on Financing Sustainable Growth<sup>[12]</sup> the Commission announced that it would carry out analytical and consultative work on the possible need to legislate in this area.

The Commission has been looking at further obstacles that hinder the transition to an environmentally and socially sustainable economy, and at the possible root causes thereof in corporate governance regulation and practices. As part of this work, two studies have been conducted which show market failures and favour acting at the EU level.

The *study on directors' duties and sustainable corporate governance* <sup>[13]</sup> evidences that there is a trend in the last 30 years for listed companies within the EU to focus on short-term benefits of shareholders rather than on the long-term interests of the company. Data indicate an upward trend in shareholder pay-outs, which increased from 20% to 60% of net income while the ratio of investment (capital expenditure) and R&D spending to net income has declined by 45% and 38% respectively. The study argues that sustainability is too often overlooked by short-term financial motives and that to some extent, corporate short-termism finds its root causes in regulatory frameworks and market practices. Against these findings, the study argues that EU policy intervention is required to lengthen the time horizon in corporate decision-making and promote a corporate governance more conducive to sustainability. To achieve this, it spells out three specific objectives of any future EU intervention: strengthening the role of directors in pursuing their company's long-term interest by dispelling current misconceptions in relation to their duties, which lead them to prioritise short-term financial performance over the long-term interest of the company; improving directors' accountability towards integrating sustainability into corporate strategy and decision-making; and promoting corporate governance practices that contribute to company sustainability, by addressing relevant unfavourable practices (e.g. in the area of board remuneration, board composition, stakeholder involvement).

The *study on due diligence requirements through the supply chain* <sup>[14]</sup> focuses on due diligence processes to address adverse sustainability impacts, such as climate change, environmental, human rights (including labour rights) harm in companies' own operations and in their value chain, by identifying and preventing relevant risks and mitigating negative impacts. The study shows that in a large sample of mostly big companies participating in the study survey, only one in three businesses claim to undertake due diligence which takes into account all human rights and environmental impacts. Therefore voluntary initiatives, even when backed by transparency do not sufficiently incentivise good practice. The study shows wide stakeholder support, including from frontrunner businesses, for mandatory EU due diligence. 70% of businesses responding to the survey conducted for the study agreed that EU regulation might provide benefits for business, including legal certainty, level playing field and protection in case of litigation. The study shows that a number of EU Member States have adopted legislation or are considering action in this field. A potential patchwork of national legislation may jeopardise the single market and increase costs for

businesses. A cross-sectoral regulatory measure, at EU level, was preferred to sector specific frameworks.

### **Objectives of this public consultation**

This public consultation aims to collect the views of stakeholders with regard to a possible Sustainable Corporate Governance Initiative. It builds on data collected in particular in the two studies mentioned above and on their conclusions, as well as on the feedback received in the public consultation on the Renewed Sustainable Finance Strategy[15]. It includes questions to allow the widest possible range of stakeholders to provide their views on relevant aspects of sustainable corporate governance.

## About you

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### \* Language of my contribution

- Bulgarian
- Croatian
- Czech
- Danish
- Dutch
- English
- Estonian
- Finnish
- French
- German
- Greek
- Hungarian
- Irish
- Italian
- Latvian
- Lithuanian
- Maltese
- Polish
- Portuguese
- Romanian
- Slovak
- Slovenian
- Spanish
- Swedish

\* Surname

de Smedt

\* I am giving my contribution as

- Academic/research institution
- Business association
- Company/business organisation
- Consumer organisation
- EU citizen
- Environmental organisation
- Non-EU citizen
- Non-governmental organisation (NGO)
- Public authority
- Trade union
- Other

\* First name

Iryna

\* Email (this won't be published)

iryna@accountancyeurope.eu

\* Organisation name

*255 character(s) maximum*

Accountancy Europe unites 51 professional organisations from 35 countries that represent 1 million qualified accountants, auditors and advisors

\* Organisation size

- Micro (1 to 9 employees)
- Small (10 to 49 employees)
- Medium (50 to 249 employees)
- Large (250 or more)

Transparency register number

*255 character(s) maximum*

Check if your organisation is on the [transparency register](#). It's a voluntary database for organisations seeking to influence EU decision-making.

4713568401-18

### \* Country of origin

Please add your country of origin, or that of your organisation.

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Democratic  
Republic of the  
Congo

Denmark

Liberia

Saint Kitts and  
Nevis

Saint Lucia

### \* Publication privacy settings

The Commission will publish the responses to this public consultation. You can choose whether you would like your details to be made public or to remain anonymous.

**Anonymous**

Only your contribution, country of origin and the respondent type profile that you selected will be published. All other personal details (name, organisation name and size, transparency register number) will not be published.

**Public**

Your personal details (name, organisation name and size, transparency register number, country of origin) will be published with your contribution.

I agree with the [personal data protection provisions](#)

If you replied that you answer on behalf of a business, please specify the type of business:

- institutional investor, asset manager
- other financial sector player (e.g. an analyst, rating agency, data and research provider)
- auditor
- other

### Consultation questions

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If you are responding on behalf of a large company, please indicate how large is the company:

- Large company with 1000 or more people employed
- Large company with less than 1000 but at least 250 people employed

If you are responding on behalf of a company, is your company listed on the stock-exchange?

- Yes, in the EU
- Yes, outside the EU

- Yes, both in and outside the EU
- No

If you are responding on behalf of a company, does your company have experience in implementing due diligence systems?

- Yes, as legal obligation
- Yes, as voluntary measure
- No

If resident or established/registered in an EU Member State, do you carry out (part of) your activity in several EU Member States?

- Yes
- No

If resident or established/ registered in a third country (i.e. in a country that is not a member of the European Union), please specify your country:

If resident or established registered in a third country, do you carry out (part of) your activity in the EU?

- Yes
- No

If resident or established registered in a third country, are you part of the supply chain of an EU company?

- Yes
- No

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

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

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

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

Please provide reasons for your answer:

A company's objective should be about continuing its operations and remaining profitable in the long term. To that end, it is critical the company understands how it affects the environment, society and its stakeholders and addresses its potential negative impacts.

Standards and guidelines developed by international organisations are available to support businesses in upholding these duties. In particular, the UN Guiding Principles on Business and Human Rights and the OECD Guidelines for Multinational Enterprises provide guidance on how to act responsibly towards stakeholders they impact.

While we have marked the first bullet point as our reply, we do not believe the word 'maximisation' is a good choice for what is asked here. ESG impacts and risks have a wide scope. The purpose of the company is not about 'maximising' but rather about having a balanced approach between its financial performance and its impact to the external environment. To add, it is unclear how we can measure such 'maximisation'.

All companies, regardless of their size should consider the above-mentioned interests in their decisions. As further explained under questions 16 and 24, smaller companies can be supported by the EC to be able to comply. The proposals should be: i) proportionate ii) taking into account the different business models, and iii) focus on businesses that pose significant risks in terms of human rights and environmental impacts.

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:

According to the findings of the Alliance for Corporate Transparency 2019 Research Report (An analysis of the sustainability reports of 1000 companies pursuant to the EU Non-Financial Reporting Directive) one-in-four companies have introduced human rights due diligence processes. [https://www.allianceforcorporatetransparency.org/assets/2019\\_Research\\_Report%20\\_Alliance\\_for\\_Corporate\\_Transparency-7d9802a0c18c9f13017d686481bd2d6c6886fea6d9e9c7a5c3cfafea8a48b1c7.pdf](https://www.allianceforcorporatetransparency.org/assets/2019_Research_Report%20_Alliance_for_Corporate_Transparency-7d9802a0c18c9f13017d686481bd2d6c6886fea6d9e9c7a5c3cfafea8a48b1c7.pdf)

The analysis indicates that 'general human rights reporting requirements are not an effective tool to ensure [...] company's management of individual risks of human rights impacts [...]. In this regard, reporting can have only a supportive role, where it ensures disclosure of meaningful information.' We support the conclusions of this analysis and we see it as a further proof that companies need to do more in the area of due diligence.

There are also other ways to ensure directors exercise their duties to balance different stakeholders' interests such as by leveraging the role of audit committees and other board functions. We further elaborate on this point in our answer to question 24.

Question 3: If you think that an EU legal framework should be developed, please indicate which among the following possible benefits of an EU due diligence duty is important for you (tick the box/multiple choice)?

- Ensuring that the company is aware of its adverse human rights, social and environmental impacts and risks related to human rights violations other social issues and the environment and that it is in a better position to mitigate these risks and impacts
- Contribute effectively to a more sustainable development, including in non-EU countries
- Levelling the playing field, avoiding that some companies freeride on the efforts of others
-

Increasing legal certainty about how companies should tackle their impacts, including in their value chain

- A non-negotiable standard would help companies increase their leverage in the value chain
- Harmonisation to avoid fragmentation in the EU, as emerging national laws are different
- SMEs would have better chances to be part of EU supply chains
- Other

Other, please specify:

We believe all the proposed benefits above are important.

In addition, an EU level framework will lead to further legislative consistency. A consistent EU legislative framework is key to achieve better economic, social and environmental outcomes. For example, corporate reporting obligations combined with corporate governance requirements will make it easier to identify, analyse and measure companies' sustainability impact. This will gradually lead to more meaningful reporting, increase transparency on companies' impact and boost capital allocation to sustainable investments.

### Question 3a. Drawbacks

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

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

Other, please specify:

Transition to a mandatory EU due diligence duty should be gradual, proportional where necessary, and supported by preparatory work to avoid negative social repercussions to local economies.

As part of our selected choices, we have also indicated the increased administrative cost. This is a logical consequence as companies are currently not bearing the cost of most externalities. Therefore, the introduction of due diligence duties will come with an additional cost compared to current cost, especially in the initial phases of implementation. Nevertheless, this is a necessary and legitimate cost of doing business. Companies doing nothing with their due diligence duties will cause much higher negative impact to the environment but also to business itself.

We have not selected the risk of disengagement from risky markets as we believe that such a development can trigger positive change and higher local standards both from an environmental and a human rights /labour perspective. Several scandals revealed in the press over the last years seem to indicate that certain companies lower their standards, e.g. on working conditions and human rights protection, precisely to stay in these markets.

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

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

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

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

other interests, please specify



the interests of society, please specify:

Although we ticked all the boxes above, companies should be able to assess the relevance of a specific interest on a case-by-case basis.

It is not realistic and feasible to take into account the interests of all stakeholders. Some of these interests may also be conflicting and consequently impossible for the company to address them all. The objective of company's governance should be linked to serving its long-term interests by preventing potential adverse impacts.

Furthermore, the Commission will have to provide clear explanations on what 'stakeholders' interests' means.

Companies should be required by law to identify their stakeholders and be transparent on the steps they take to address their interests. This will allow shareholders, stakeholders and regulators to assess and, if necessary, challenge the company's analysis and decisions. Nevertheless, each company is best placed and should remain responsible for identifying its stakeholders. The EC cannot impose a one-size-fits-all legal regime to do so.

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	<input checked="" type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Management of the risks for the company in relation to stakeholders and their interests, including on the long run	<input checked="" type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Identification of the opportunities arising from promoting stakeholders' interests	<input checked="" type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>

Please explain:

Corporate directors are best placed to assess opportunities that may arise from promoting stakeholders' interests and how this can contribute to the resilience and viability of the company. Requirements to do this

by law would reduce potential pressure received to focus on short term profit-oriented management. These requirements would be equally useful and appropriate for the public sector.

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

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

Please explain:

We agree that a requirement to identify, prevent and address risk and adverse impact is necessary and should be accompanied by tangible measures. Using KPIs and targets can be part of a framework embedding such a process, but it might not be necessary for all cases. In this context, we believe it should be up to the company to define the relevant KPIs, targets and be transparent about it.

To be able to propose such a requirement, the EC should provide more details by for example i) specifying the relevant criteria (materiality, measurable, appropriate etc.) ii) use of specific KPIs (and at later stage targets) as defined by EU reporting obligations.

Overall, we believe that sustainable value creation should be integrated into the duties of corporate directors. They need to consider the full range of factors used in the value creation process in a holistic way. Measuring effective progress requires thorough analysis of the impacts that business activities generate in its own operations and throughout the entire supply chain. Such holistic approach to risk management is an important opportunity for businesses to innovate and attract new customers and markets.

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:

Any legislation should be clear on what directors' duty of care means in practice. We believe the word 'balancing', which does not equal to 'take into account/address the interests of all stakeholders', is a better and more realistic approach. Companies need to be specific and transparent on how they balance different stakeholders' interests and their mission.

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?

Directors' liability

Directors may not welcome legal liability for failure to adhere to the duty of care or due diligence duty. Too heavy responsibilities and excessive liability risk may render directors too compliance oriented and risk averse. Conversely, over-protecting them may reduce their sense of responsibility and hamper the public interest. It is key to strike the right balance to ensure the desired changes in the corporate environment.

Balancing stakeholders' interests

Balancing stakeholders' interests can pose practical challenges. It may not be feasible for the company to meet the interests of all stakeholders. When identifying its negative impacts on stakeholders and the environment, a company needs to take a holistic approach and more importantly remain transparent on the followed processes.

How could these possible risks be mitigated? Please explain.

Clarify reasonable duty of care

To mitigate the risk of divergent interpretations, legislation needs to be very clear on what directors' duty entails when we refer to stakeholders' interests. A 'clear' due process can help companies assessing better stakeholders' interests especially in case any stakeholders group claim their interests are not taken into account.

Balancing stakeholders' interests

It is not realistic to expect from a company to address the interests of all stakeholders. For this reason, it is helpful for companies to remain transparent on their processes and remain in close contact and dialogue with their key stakeholders.

Establish a level playing field

Another way to mitigate potential risks is establishing a level playing field. Introducing mandatory duties for all companies will reduce strategies aimed at benefiting from non-compliance and help foster responsible behaviour equally across all businesses. Investors and companies themselves call for a level playing field in line with the EC Study on due diligence requirements through the supply chain.

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

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

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

Please explain:

Sustainability risks, impacts and opportunities should be an integral part of a company's core strategy and not an add-on by means of a separate sustainability strategy. Sustainability impacts will one way or another impact the company's long-term viability. Boards should be accountable for ensuring that environmental, social and governance factors are integrated with financial performance. Corporate governance over sustainability risks, impacts and opportunities should be established as for any other material business aspect.

**Enforcement of directors' duty of care**

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

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

Please describe examples:

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

Please explain your answer:

The EC should provide more clarity/details on what the following means: 'civil society organisations should be given a role in the enforcement of directors' duty of care'. This wording does not clarify to which extent/in which way stakeholders should be involved in companies' decision making. Undoubtedly, stakeholders have the right to pursue their interests. Nevertheless, their involvement should not result in a 'paralysing' behaviour on behalf of the companies, e.g. conflicting interests that inhibit directors from taking any action.

Legislation at EU level should focus more on outcomes, effective enforcement of rules and behavioural change. In addition to rulemaking, regulators can use complementary approaches, such as research, awareness raising, education, incentives, reporting, benchmarking, labelling, etc.

The EC may draw on lessons from the French experience with its Corporate Duty of Vigilance Law. The French experience indicates a number of practical challenges with enforcement such as the lack of legal certainty on many aspects of due diligence which may hamper its enforcement e.g. regarding risk mapping frequency and what constitutes a breach.

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.

Incorporating feedback from affected stakeholders will be vital to ensure the duty of care is respected. Companies should engage with stakeholders who are affected by their operations, collect their input and amend accordingly their decision making. Companies themselves are best placed to identify the relevant stakeholders as long as they remain transparent on the procedures they follow.

## Section III: Due diligence duty

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For the purposes of this consultation, "due diligence duty" refers to a legal requirement for companies to establish and implement adequate processes with a view to prevent, mitigate and account for human rights

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

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

We agree with the above EC definition.

The definition should also detail if due diligence obligations should cover the entire supply chain i.e. how far down in the value chain one should go including the use of 3rd party suppliers and their contract parties, i.e. the indirect supply chain. Companies with a supply chain outside of the EU will require specific guidance to fulfill their due diligence obligations.

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

- Option 1. "Principles-based approach": A general due diligence duty based on key process requirements (such as for example identification and assessment of risks, evaluation of the operations and of the supply chain, risk and impact mitigation actions, alert mechanism, evaluation of the effectiveness of measures, grievance mechanism, etc.) should be defined at EU level regarding identification, prevention and mitigation of relevant human rights, social and environmental risks and negative impact. These should be applicable across all sectors. This could be complemented by EU-level general or sector specific guidance or rules, where necessary
- Option 2. "Minimum process and definitions approach": The EU should define a minimum set of requirements with regard to the necessary

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

- Option 3. “Minimum process and definitions approach as presented in Option 2 complemented with further requirements in particular for environmental issues”. This approach would largely encompass what is included in option 2 but would complement it as regards, in particular, environmental issues. It could require alignment with the goals of international treaties and conventions based on the agreement of scientific communities, where relevant and where they exist, on certain key environmental sustainability matters, such as for example the 2050 climate neutrality objective, or the net zero biodiversity loss objective and could reflect also EU goals. Further guidance and sector specific rules could complement the due diligence duty, where necessary.
- Option 4 “Sector-specific approach”: The EU should continue focusing on adopting due diligence requirements for key sectors only.
- Option 5 "Thematic approach": The EU should focus on certain key themes only, such as for example slavery or child labour.
- None of the above, please specify

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

We believe at this stage a principles-based horizontal approach should be prioritised; it should be the company's responsibility to determine if this should be further coupled with a theme or sector specific approach. The themes which could be combined with a horizontal approach can be plenty and it will be challenging for the EU to prioritise which are the most pertinent for the companies (e.g. it can vary from child labour to waste discharge, and others). It will be useful nevertheless if the EC issues relevant guidance.

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

We believe that a “principles-based approach” as detailed in option 1 should be defined at EU level (including identification, prevention and mitigation of relevant human rights, social and environmental risks and negative impacts). A principles-based approach can be applied by various sectors and accordingly lead to a level playing field. It can also enhance exchange of best practices.

At a later stage, this can be combined with specific themes decided by the companies and sector specific guidance by the EC where necessary.

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

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

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

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?

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

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

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

Please explain your choice, if necessary

All companies impact their external environment and should be encouraged to advance on a sustainable path. It is not only about a company's size but more about a company's risk profile. There are businesses that may have a few employees but still a negative environmental impact.

To reduce potential burden on SMEs, we support the following approach: 1) Include medium sized businesses in the riskiest sectors within the scope. 2) As risky sectors can be further categorized (less or more risky), we propose to provide medium companies of less risky sectors an additional delay of 2 years (in comparison to other businesses). That way, these medium sized businesses can rely on the experiences and best practices taken by their peers in the riskier sectors. 3) Smaller businesses with fewer than 50 employees should be encouraged to adopt voluntary approaches to due diligence requirements.

Accountancy Europe stands ready to support the Commission in its work to define how risky/less risky sectors would be defined. It will take further work and time for most of them to build up their monitoring, control and reporting mechanisms in this area.

We strongly encourage the Commission to come up with non-binding guidelines that could be applied by all categories of SMEs – from micros to medium sized ones.

Capacity building support, including crucially financial support is key to build up due diligence maturity for SMEs. When devising such capacity building schemes, the role of key SME intermediaries and advisors, such as accountants and chambers of commerce, should be acknowledged and fostered. These advisors are in regular contact with SMEs and have the expertise and 'reach' to help build up their SME clients' due diligence maturity. Accountancy Europe recently published a paper looking specifically into the ways in which SME accountants could support SMEs to move towards more sustainable business practices: (<https://www.accountancyeurope.eu/publications/sme-risk-management-sustainability/>)

Finally, we would like to propose providing a 'good manufacturer scheme/label/certificate' to enable ethical SMEs to source goods and services from "accredited" sources (ideally at EU level). Compliance with this label/certificate scheme can be further ensured through appropriate assurance and verification requirements on the third country provider/manufacturer.

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

- Yes
- No
- I do not know

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

We believe that third country companies should be subject to the same rules as the EU ones when they do business in the European market. This will be key to establish a level playing field and preserve EU's competitiveness while encouraging a global transition. The rest of the measures as asked in this question as well as in 17b and 18 should be further discussed with the relevant stakeholders.

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

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:

As it is primarily the duty of countries to protect workers, environment etc., the EC should ensure through trade measures that trading partners (countries) implement laws and regulation that are comparable to EU provisions.

Question 19: Enforcement of the due diligence duty

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

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

Please provide explanation:

We believe that supervision at national level is necessary to ensure due diligence duty enforcement. Supervisors need to be properly equipped and resourced while the rules they will be assessing need to be clear and consistent across Europe.

If different national organisations are involved, they should be closely connected, for instance in a European network (based on the model of competition authorities). A European body should be responsible for ensuring coordination and implementation.

Once rules are in place, enforcement is largely a matter for Member States. Therefore, the EC should step up its oversight of Member State' enforcement policies and make this an important element of its infringement policy.

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:

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

## Section IV: Other elements of sustainable corporate governance

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Question 20: Stakeholder engagement

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

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

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

Please explain.

Directors need to engage with and draw on feedback from relevant stakeholders.

Any requirements regarding stakeholder engagement should be principles-based and not prescriptive. The

EC should set the parameters within which companies should operate. In addition, the EC should allow companies to determine themselves the best mechanisms to engage with their stakeholders (based on their business model and circumstances).

Importantly and as flagged before, companies should be transparent on the mechanisms they use to identify and engage with their stakeholders and how they take their interests into account.

Stakeholders should be able to file a complaint with the national regulator should i) available information is not sufficient or reliable and ii) there has been no further action by the company to remedy this. Regulators should be able to make inquiries of corporates about the quality of information and take steps accordingly (cf. Kingman Review).

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

As previously flagged, companies should be able to map out their own relevant stakeholders on the condition they remain transparent on their strategy and actions.

**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	<input type="radio"/>	<input type="radio"/>
Stakeholder general meeting	<input type="radio"/>	<input type="radio"/>
Complaint mechanism as part of due diligence	<input checked="" type="radio"/>	<input type="radio"/>
Other, please specify	<input checked="" type="radio"/>	<input type="radio"/>

**Other, please specify:**

Best practices can vary by company, industry, and country. The focus should be on what needs to be done and not on prescribing how to do this. The EC should facilitate best practice sharing by collecting and giving access to information on existing practices.

A complaint mechanism can be useful as part of their stakeholder engagement system. The focus should not be only about the potential complaints/breaches. Stakeholder engagement can have a bigger effect as it offers the company the opportunity to improve its decision making.

Another possible mechanism could be a platform or a stakeholder panel where companies can engage with stakeholders. This mechanism needs to be transparent with the followed procedures and outcomes and needs to be combined with a timeframe on actions.

**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 [17] (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	
Requirement to include carbon emission reductions, where applicable, in the	

lists of sustainability factors affecting directors' variable remuneration	
Taking into account workforce remuneration and related policies when setting director remuneration	
Other option, please specify	
None of these options should be pursued, please explain	

Please explain:

Currently the non-financial aspect is not reflected in many directors' remuneration schemes, and where it is, it is not on the same level as the achievement of financial targets. Directors' remuneration should be contingent on non-financial performance and in line with the Board's decisions.

Non-financial KPIs and targets as set by the company should be integrated into directors' remuneration schemes. One way forward would be: a remuneration committee defining respective KPIs and determine accompanying measures (e.g. via benchmarking). Nevertheless, companies should be given the discretion to decide on the means of achieving non-financial targets. For this reason, we have left the above choices without ranking.

## 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 [18] (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

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

Please explain:

Boards need to have relevant and up-to-date sustainability expertise to be able to make proper business decisions.

While we support the need for mandatory requirements, agreeing on specific numbers/percentages will be challenging. The need on competences and expertise can be sector or even company specific.

Boards need to review their business model and think in new ways about risk management and resilience. This requires diverse skills, knowledge, backgrounds, expertise, profiles and goes beyond just having sustainability expertise.

The board should regularly assess whether its diversity and expertise remain relevant and up to date. To achieve this, regular trainings -amongst others- will be key.

### 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[19]. (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:

We invite the Commission to ensure legislative consistency. Specifically, the scope of the EU legislation on sustainable corporate governance should be consistent with the revision of the Non-Financial Reporting Directive provisions and sustainable finance agenda to ensure an aligned approach to directors' duties and due diligence at capital markets level across Europe. Non-financial reporting combined with changes at governance level will deliver more meaningful and consistent non-financial reporting.

The proposals should be proportionate and take into account the specificities of each company, its business model and particularly focus on those businesses that pose material risks in terms of human rights and environmental impacts. The Commission should also consider how this will affect the financial sector, as institutional investors expect non-financial information from their clients.

The role of audit committees as well as other relevant board committees, risk management and company's internal controls are additional ways of fulfilling the sustainable corporate governance agenda.

Audit committees in specific have the potential of: i) overseeing processes on non-financial metrics ii) supporting the board with achieving a sustainable long-term strategy iii) considering stakeholders' interests. Audit committees should develop further and acquire broader expertise on sustainability matters and non-financial risk management.

Certain companies have set up separate CSR/sustainability committees. However, we believe that sustainability should be integrated in other relevant committees (i.e. risk, remuneration, audit) rather than in a stand-alone sustainability committee, where it risks being siloed and inefficient.

## Section V: Impacts of possible measures

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

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

Table

	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 linked 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).

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