Contribution ID: f25702f0-6221-44f2-be33-ad8020843854
Date: 08/02/2021 16:20:46

# Consultation Document Proposal for an Initiative on Sustainable Corporate Governance

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This document is a working document of the Commission services for consultation and does not prejudge 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

**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[11] 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[12] 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* [13] 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[14] 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

* 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

Lueck

* 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

Maximilian

* Email (this won't be published)

lueck@dai.de

* Organisation name

*255 character(s) maximum*

Deutsches Aktieninstitut e.V.

* 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.

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* Country of origin

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

- Afghanistan
- Åland Islands
- Albania
- Algeria
- American Samoa
- Andorra
- Angola
- Anguilla
- Antarctica
- Antigua and Barbuda
- Argentina
- Armenia
- Aruba
- Australia
- Austria
- Azerbaijan
- Bahamas
- Bahrain
- Bangladesh
- Djibouti
- Dominica
- Dominican Republic
- Ecuador
- Egypt
- El Salvador
- Equatorial Guinea
- Eritrea
- Estonia
- Eswatini
- Ethiopia
- Falkland Islands
- Faroe Islands
- Fiji
- Finland
- France
- French Guiana
- French Polynesia
-
- Libya
- Liechtenstein
- Lithuania
- Luxembourg
- Macau
- Madagascar
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- Mali
- Malta
- Marshall Islands
- Martinique
- Mauritania
- Mauritius
- Mayotte
- Mexico
- Micronesia
- Moldova
- Saint Martin
- Saint Pierre and Miquelon
- Saint Vincent and the Grenadines
- Samoa
- San Marino
- São Tomé and Príncipe
- Saudi Arabia
- Senegal
- Serbia
- Seychelles
- Sierra Leone
- Singapore
- Sint Maarten
- Slovakia
- Slovenia
- Solomon Islands
- Somalia
- South Africa
- South Georgia and the South

| | | | |
|---|---|---|---|
| | French Southern and Antarctic Lands | | Sandwich Islands |
| Barbados | Gabon | Monaco | South Korea |
| Belarus | Georgia | Mongolia | South Sudan |
| Belgium | Germany | Montenegro | Spain |
| Belize | Ghana | Montserrat | Sri Lanka |
| Benin | Gibraltar | Morocco | Sudan |
| Bermuda | Greece | Mozambique | Suriname |
| Bhutan | Greenland | Myanmar /Burma | Svalbard and Jan Mayen |
| Bolivia | Grenada | Namibia | Sweden |
| Bonaire Saint Eustatius and Saba | Guadeloupe | Nauru | Switzerland |
| Bosnia and Herzegovina | Guam | Nepal | Syria |
| Botswana | Guatemala | Netherlands | Taiwan |
| Bouvet Island | Guernsey | New Caledonia | Tajikistan |
| Brazil | Guinea | New Zealand | Tanzania |
| British Indian Ocean Territory | Guinea-Bissau | Nicaragua | Thailand |
| British Virgin Islands | Guyana | Niger | The Gambia |
| Brunei | Haiti | Nigeria | Timor-Leste |
| Bulgaria | Heard Island and McDonald Islands | Niue | Togo |
| Burkina Faso | Honduras | Norfolk Island | Tokelau |
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| Cambodia | Hungary | North Korea | Trinidad and Tobago |
| Cameroon | Iceland | North Macedonia | Tunisia |
| | | | |

- Canada
- Cape Verde
- Cayman Islands
- Central African Republic
- Chad
- Chile
- China
- Christmas Island
- Clipperton
- Cocos (Keeling) Islands
- Colombia
- Comoros
- Congo
- Cook Islands
- Costa Rica
- Côte d’Ivoire
- Croatia
- Cuba
- Curaçao
- Cyprus
- Czechia
- India
- Indonesia
- Iran
- Iraq
- Ireland
- Isle of Man
- Israel
- Italy
- Jamaica
- Japan
- Jersey
- Jordan
- Kazakhstan
- Kenya
- Kiribati
- Kosovo
- Kuwait
- Kyrgyzstan
- Laos
- Latvia
- Lebanon
- Lesotho
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- Oman
- Pakistan
- Palau
- Palestine
- Panama
- Papua New Guinea
- Paraguay
- Peru
- Philippines
- Pitcairn Islands
- Poland
- Portugal
- Puerto Rico
- Qatar
- Réunion
- Romania
- Russia
- Rwanda
- Saint Barthélemy
- Saint Helena Ascension and Tristan da Cunha
- Turkey
- Turkmenistan
- Turks and Caicos Islands
- Tuvalu
- Uganda
- Ukraine
- United Arab Emirates
- United Kingdom
- United States
- United States Minor Outlying Islands
- Uruguay
- US Virgin Islands
- Uzbekistan
- Vanuatu
- Vatican City
- Venezuela
- Vietnam
- Wallis and Futuna
- Western Sahara
- Yemen
- Zambia
- Zimbabwe

Democratic Republic of the Congo

Saint Kitts and Nevis

- Denmark
- Liberia
- 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

If other, please specify:

Replies are given from the perspective of capital markets oriented corporates, mainly listed on regulated markets.

## Consultation questions

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

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:

Deutsches Aktieninstitut regrets that the consultation is in many instances not framed in a way as to allow full expression of the different views of all stakeholders affected by the issue at hand. This is unfortunate as ideas contemplated in this consultation can be far-reaching and deserve the full range of opinions being reflected.

Question 1 is one example of the flawed design of the consultation. We believe that companies already take into account the aspects mentioned in the question, beyond what is currently required by EU law. This because of their own initiative or, because the law at Member State level requires them to do so. We thus think that the role of the EU legislator is not necessary or at least minimal. None of the options presented leave room to reflect this view. In case most respondents answer according to the two first options (as Deutsches Aktieninstitut does), it could thus be interpreted by DG Jusitice as the need for EU legislative activities in this field. The answer to the question feels like a trap as respondents potentially express views they may not have. This is not the purpose of a public consultation, which is to form a comprehensive base for decision, including the full range of views of stakeholders affected.

Also, later in the questionnaire a strong need for the differentiation between directors and executives become striking in order to fully comprehend the possible impacts of a proposal implied in the questions. Therefore, more effort to differentiate between one-tier and two-tier board systems would have been indispensable.

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:

Such a framework should not be overly descriptive in order to leave flexibility to companies in setting up their bespoke risk mitigation processes. In order to enhance legal certainty, the framework should however at the same time set out minimum requirements on due diligence processes as well as definitions. For this, harmonization of divergent national legislation might be necessary. The framework should clearly define the scope as well as the company's obligations and when it can be released from liability. In addition, in order for a legal framework to be effective it should be practical, tangible and realistic to implement. The reference document that should be consulted in order to build a worldwide acceptable framework are the UN Guiding Principles on Business and Human Rights. The minimal standards and definitions should apply to all sectors alike and could be combined with topic or sector specific regulations in situations/sectors with high human rights violations risks.

The EU framework should be proportionate and hence only address the contractual relationship between the company and the first tier supplier instead of being mandatory along the entire supply chain.

The scope should be confined to human rights violations. There is a risk that if the proposal becomes too overarching in scope that human rights will become a secondary consideration, which must be avoided. Any EU legislative framework should be closely aligned with the UN Guiding Principles on Business and Human Rights, also to avoid the risk of fragmentation in the EU, as emerging national laws are already different. European companies operating worldwide already refer to these standards to conduct business in a responsible way and would provide legal certainty for companies as regards their obligations.

In addition, the framework should not contradict sector specific rules already in place on the EU-level, such as the European regulation on conflict minerals. It should be coherent to already existing EU legislative acts addressing human rights. In this regard, the ongoing review on the non-financial reporting directive should be particularly taken into account.

EU companies should moreover not be required to set up a due diligence process for suppliers solely based in the European Union.

The future EU framework should also be applicable to non-EU companies operating within the EU to

ensure a level playing field. Due to the importance of human rights and largely global value chains, we further advocate for multilateral solutions. Such a broad legal framework could be prepared by an EU initiative, which, as a pioneer, provides a strong impetus in order to then involve as many other states as possible.

Last, the issue of liability needs to be addressed: The EU framework can only require companies to make best efforts to avoid violations of human rights. It should also refrain from granting third parties (eg non-governmental organizations) a right to bring actions against the company or the management of a company before national courts.

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:

Beyond the importance of harmonization, we also want to emphasize that any EU legislative action should seek alignment with international principles, such as UN guiding principles. This is of paramount for globally operating EU companies. European companies operating worldwide already refer to these standards to conduct business in a responsible way and would provide legal certainty for companies as regards their obligations. Furthermore, due to the importance of human rights and largely global value chains, we advocate for multilateral solutions for legislative measures. Such a broad legal framework could be prepared by an EU initiative, which, as a pioneer, provides a strong impetus in order to then involve as many other states as possible. Having a harmonized approach at EU level would also ensure a level playing field for all companies operating in the Single Market and ensure an effective implementation of the ultimate goal -

protection of human rights in the supply 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)?

- [x] Increased administrative costs and procedural burden
- [ ] Penalisation of smaller companies with fewer resources
- [x] Competitive disadvantage vis-à-vis third country companies not subject to a similar duty
- [x] Responsibility for damages that the EU company cannot control
- [x] Decreased attention to core corporate activities which might lead to increased turnover of employees and negative stock performance
- [x] 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
- [x] Disengagement from risky markets, which might be detrimental for local economies
- [x] Other

Other, please specify:

There might arise difficulties for the expansion of renewable energies because of problematic supply chains with regards to pv panels or raw materials. With a sensible formulation of the law, we can avoid the points listed above. It should also be avoided that there is a trade-off between various sustainability goals, such as human rights and climate protection.
In case of a too strict EU framework, we also see the risk of disengagement from countries from their duties to protect the environment, human rights, social rights. Those duties will be conferred to companies despite them being core state tasks.
As mentioned above, undue legal liability risks can be expected, which is why any EU legislative action should set out necessary limitations for legal actions against companies. We therefore call for a legal regulatory framework which clearly defines a company's obligations and when it can be released from liability.
Last, mandatory due diligence could also create a climate of distrust and defensive behaviours: the fear of being held liable with regard to their supply chains could lead EU companies to become very cautious to avoid legal risks rather than engage trustfully in useful dialogue and cooperation.

## 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 | ◉ | ○ | ○ |
| the interests of employees | ◉ | ○ | ○ |
| the interests of employees in the company's supply chain | ○ | ○ | ◉ |
| the interests of customers | ◉ | ○ | ○ |
| the interests of persons and communities affected by the operations of the company | ○ | ○ | ◉ |
| the interests of persons and communities affected by the company's supply chain | ○ | ○ | ◉ |
| the interests of local and global natural environment, including climate | ○ | ○ | ◉ |
| the likely consequences of any decision in the long term (beyond 3-5 years) | ○ | ○ | ◉ |
| the interests of society, please specify | ○ | ○ | ◉ |
| other interests, please specify | ○ | ○ | ◉ |

the interests of society, please specify:

other interests, please specify:

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 agree | I disagree | | | I do not |
|---|---|---|---|---|---|---|

| | I strongly agree | to some extent | to some extent | I strongly disagree | I do not know | take position |
|---|---|---|---|---|---|---|
| Identification of the company´s stakeholders and their interests | ○ | ○ | ○ | ◉ | ○ | ○ |
| Management of the risks for the company in relation to stakeholders and their interests, including on the long run | ○ | ○ | ○ | ◉ | ○ | ○ |
| Identification of the opportunities arising from promoting stakeholders' interests | ○ | ○ | ○ | ◉ | ○ | ○ |

Please explain:

All of the above mentioned points are part of the successful management of a company and are therefore a core interest of the directors of the company themselves. For this reason, we do not see a need for additional regulatory measures. In addition, some of the above mentionend measures are already part of the national governance codes. We therefore believe that it is appropriate for the directors to take these into account in their decision-making, but not for this to be required by law. So, no regulatory action required to set an incentive here. But it seems that no incentive but a threat of legal liability is aimed at, here. A lot of formal mistakes can arise in the identification and analyzing process. Especially in combination with Question 5 and 7, the resemblance to a political process of decision making is striking (see answer to Q7). Secondly, some of the issues mentioned are already tackled by national governance codes and the non-financial reporting directive and hence do not require further legislative action. Third, many of the issues mentioned above are also already addressed by national corporate governance codes, which is the right place to do so. Last, it is important to note that there are various ways to identify stakeholders, and that stakeholders can differ from one company to the other. A one size fits all approach is thus not warranted and it should remain the decision of the company to define its relevant stakeholders.
We therefore believe that it is appropriate for the directors to take these into account in their decision-making, but not for this to be required by law.

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:

Please be aware that corporate directors are not in charge of ‘setting up adequate procedures’ but they only oversee such procedures. The supervisory board also does not set up targets for the management board in the dualistic system.
As mentioned above and in our answer to Q13 the proposal introduces a requirement that probably cannot be fulfilled as there is no restriction on “relevant” stakeholders and “relevant” interests or impacts. It is not possible, we would say, to identify every single person and to consider every possible negative impact on them. There would have to be a limitation in any way to make such requirement operable.
Especially, it would have to be elaborated further, if “directors” have the duty to prevent any adverse impact on stakeholders. What would that mean in practice? If, e.g. the company has obtained a permit to build a plant this is the result of considerations of different interests by the legislator and in executing the laws in the individual case, by the authorities. When setting up the respective law, the legislator has decided that citizens have to generally bear that plants may be built and probably environmental conditions were imposed to compensate for this. What is, in the notion of the EU Commission, the relationship between the legal “can” as result of legislative process and its execution and the duty to avoid impacts?
Isn’t this also contradicting the concept of balancing the interest of stakeholders? As we interpret it, the aim is to achieve a balance of conflicting stakeholders’ interests that is as gentle as possible. But still, also in such concept, which we disagree with as a legal concept, all interests cannot be fulfilled fully and so, negative impacts cannot be avoided entirely, a compromise has to be found. The aim is probably to achieve a balance that is as gentle as possible. But here, a duty to prevent any negative impact on stakeholders is imposed.

If the EU Commission does not refrain from such due diligence procedure concerning managerial decisions, we would recommend to at least limit the law to human rights and the responsibility for appropriate due diligence processes in the company.

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 phrasing of the question is biased. It is tendencious in the way that it suggests that the balancing of the interests of all stakeholders would be the prefereable way and currently “directors” focus on short-term interests of shareholders. There can for instance be situations where short-term decisions need to be taken in order to preserve the long-term value creation- for the sake of stakeholders (eg employees). Indisputably

existing short-term interests of the company (like cash flow etc.) are not even mentioned. It does not differenciate, but presents two (seamingly opposing) alternative situations to decide upon. However, the situations outlined are too simplistic.
The concept of the company interest, here, is presented in a way that we know from the political process. Since there is no objectifiable or preset common good respectively public interest for politics to pursue, but only a collection of particular interests of the various actors, a democratic system tries to bring them into a balance that satisfies all actors sufficiently. Economic decision-making seeks solutions in terms of an optimal expenditure of resources for a given outcome. The rationality is not set directly by law but firstly derived from the company statute as being a commercial entreprise. This is why it is already here questionable that as pre-condition all interests would have to be put on the same level. Secondly, for listed companies the rules of the capital market give incentives for certain behaviour like always having an eye on the stock price in order not to become a target of a hostile takeover. Sharehoders have influence on board members via the election process and their say on pay and so incentivises management, which has recently even been strenghthend by EU law. So, none of the relevant framework is basically changed by the current proposals. But the behavior of relevant actors is already changing. This is due to a bundle of reasons (may it be reputational, instrinsic, risk management, regulatory, or governance codes driven) and a combination hereof. The driver of the change is, as we have tried to explain, not company law. And the concept is not apt to become one: the concept of the interest of the company is not objectifiable and decisions aiming at it enjoy broad discretion, that courts will respect to the limit of abuse instead of second-guessing the decision. The concept cannot serve as a positive guidance for decisions. It leaves all the important questions how to use the discretion granted to the decision-makers unanswered.
Excessive personal obligations lead to extensive reporting without the measures being effective. Therefore, this should not be covered by a director's duty of care. Furthermore, we think that this is part of the entrepreneurial freedom of the directors and not prescribed by any legislation.

## 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?

It is almost impossible to define all interests and restrictions of business activities and decisions. A law in this regard could also have a negative impact on fundamental principles of freedom of enterprise for example.

The main risks of an approach as described in question 8 are civil liability, bureaucracy and inability in decision-making. Stakeholders, who deem their rights not being balanced in the right way, might seek to bring an action against the company or management before a court. This would be utterly disproportionate as we explain in our answer to Q13.

## How could these possible risks be mitigated? Please explain.

The risks can be mitigated by refraining from having the definition and especially the combination with the proposals in Q7 and Q13 laid down in EU law. Moreover, we believe that the Corporate Governance Codes are the best forum to deal with this topic.

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

It depends on the situation. The wide integration of stakeholder interests can be indicated in a specific situation and find support from shareholders. In some cases however, the wide integration of stakeholder interests might not indicated and even harmful to the company in a given situation and hence not find support by shareholders.

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:

Deutsches Aktieninstitut wonders, where the assumption of the above question that companies do not integrate these issues into their strategy stem from. It is not accompanied by concrete, unbiased evidence, which is irritating and does not adhere to the better regulation standards of the European Commission.

Before making such statements, the European Commission should rather assess the committment companies are already now displaying, for instance by following national corporate governance codes or the requirements of the non-financial reporting directive.
Finally, in the dual board system the members of the supervisory board are not in charge for setting up the strategy. We think it should be up to the management board members to decide on taking these considerations into account, and that they should not be required to do so by law.

**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:

As stated above, the concept of the interest of the company with the duty to balance all interests is not apt to be a a positive guidance for a better decision making, as framed in the introduction of this questionnaire, nor for court second-guessing of managment decisions. Therefore, we believe, the proposal aims at unattainable complete compliance with formal and procedural requirements (identifying all stakeholders, balancing all interests, science –based targets), in order to enable holders of particular interests of civil society to question every decision and sue management personally and put them in constant threat. This is a pity because we believe that this will slower down the transitional process of the economy.

Moreover, the concept is unclear. For example, we wonder how courts would rule in such enforcement cases. Would the business judgement rule apply or would courts examine if the weight given to the stakeholder interest was adequate, so second-guess the decision? As there is no guidance for courts other than finding an abuse of the discretion of the directors, we wonder what concept the EU-Commission follows in the enforcement of directors' duties.

Also, as already stated above, in our view the relation of state permits for certain company actions should be taken into account as such permits, e.g. to built a new plant, are already the result of considerations of different interests by the legislator and in executing the laws in the individual case, the authorities. What is the relation between action on the basis of permits by authorities and the enforcement of directors' duties by third parties? Isn't the authority of the legislator questioned by such an enforcement process?

We thus strongly disagree to grant the above mentioned groups a role in the enforcement of due diligence obligations. It would breach with the basic legal principles mentioned above. It would furthermore create the risk that competitors abuse this tool to cause harm (in engaging straw men pretending to be affected stakeholders).

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

## Section III: Due diligence duty

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

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

We disagree with this definition. The extension of a “due diligence duty” on health and, in particular, environmental impacts inevitably leads to legal uncertainty, because virtually every service/purchased product in some way or another has a (negative) effect on health and environment (e.g. noise/emissions etc.). More so, taking into account the broad definition of a supply chain, it becomes virtually impossible to evaluate every business relationship on its impact on health and environmental impacts. It is difficult to establish a direct link between the act of a particular company and the global phenomenon of climate change.

As a consequence, we recommend to narrow down the definition of a due diligence duty to “human rights” which– implicitly – also extents to severe health and environmental issues, but excludes a due diligence duty for socially recognized health and environmental issues. This brings the advantage that the due diligence duty, first of all, becomes more manageable for companies and, second, more effective. A rather broad definition, on the other hand, is in danger of being ineffective, because companies might focus on different /wrong effects of their actions.
To establish a meaningful, practical and proportionate due diligence duty on EU level, further limitations are necessary. This relates first of all to the notion of « business relationships » as determining factor for the « supply chain ». The notion is too broad and too unprecise. The term « supply chain » should be limited to first tier suppliers only, as it is simply impossible for companies to ensure compliance with EU standards along the entire supply chain, which includes suppliers, with whom no contractual relationship exists. Even for first tier suppliers, there needs to be included safeguards for companies that do not have the necessary contractual power to impose EU standards on their suppliers (eg European SME, whose first tier supplier is Samsung).
It should also be underlined that mandatory due diligence should focus on the supply chain upstream (direct subcontractors or providers) and not midstream (e.g., JV partners) or downstream (e.g., distributors, clients and consumers). Due diligence in relation to the use of products by clients would be difficult to achieve because it would require companies to dictate the consumption habits and practices of other companies and

individuals. With regard to professional customers, it would generate overlapping obligations because the supplier would try to apply its own due diligence regarding the customer whereas the customer would apply its own due diligence regarding the supplier.

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?

Deutsches Aktieninstitut is in favour of a horizontal approach comprising all sectors. The framework could however be complemented with topic or sector specific regulations in situations/sectors with high human rights violations risks.

As regards to the themes covered, we suggest to limit them to human rights, excluding environmental and social issues. This shall by no means imply that companies do not respect the latter issues. To the contrary : many companies are especially in the field of combatting climate change front runners, being involved in numerous voluntary cross-industry initiatives.  The exclusion of climate change issues is due to the fact that it is hard to establish a direct link to the company in question, thereby creating legal uncertainty.

Minimum process and definitions approach: The framework should set out minimal requirements on due diligence processes as well as definitions. For this, harmonization of divergent national legislation might be necessary. The framework should define the scope, a company’s obligations and when it can be released from liability. At the same time, the framework should not be too prescriptive, thereby leaving flexibility to EU companies, taking into account their specific situation.

It should be specified that the due diligence duty is an obligation of means rather than results because it is impossible to guarantee “zero risk” on the supply chains. Even the best sustainability audit carried out at a given time does not ensure that a moment later the level of compliance with contractual clauses will not significantly decrease for reasons that cannot always be anticipated or monitored.

It should also clarify that its focus should be on the most severe risks, in a risk-based approach, taking into account the fact that it is impossible to mitigate every single risk on the supply chains. Due diligence is an ongoing process which has to be improved over time focusing first on the most salient risks before analysing less important risks.

In addition, in order for a legal framework to be effective it should be practical, tangible and realistic to

implement. The reference document that should be consulted in order to build a worldwide acceptable framework are the UN Guiding Principles on Business and Human Rights. Those minimal standards and definitions should apply to all sectors alike and could be combined with topic or sector specific regulations in situations/sectors with high human rights violations risks.

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.

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)

- [x] Human rights, including fundamental labour rights and working conditions (such as occupational health and safety, decent wages and working hours)
- [x] 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
- [x] Other, please specify

Other, please specify:

A clear a focus on human rights should be the principle aim of any legislative proposal. There is a risk that if the proposal becomes too overarching in scope that human rights will become a secondary consideration, and this must be avoided.
Any EU legislative framework should be closely aligned with the UN Guiding Principles on Business and Human Rights, also to avoid the risk of fragmentation in the EU, as emerging national laws are already different. European companies operating worldwide already refer to these standards to conduct business in a responsible way and would provide legal certainty for companies as regards their obligations.

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?

We urgently recommend that the legislature clearly defines the concept of adverse impacts on human rights in order to create legal certainty for all parties involved.
Definitions on the scope of the obligation and the content of the obligation are essential to be covered.

It should be specified that the due diligence duty is an obligation of means rather than results because it is impossible to guarantee “zero risk” on the supply chains. Even the best sustainability audit carried out at a given time does not ensure that a moment later the level of compliance with contractual clauses will not significantly decrease for reasons that cannot always be anticipated or monitored.
It should also clarify that its focus should be on the most severe risks, in a risk-based approach, taking into account the fact that it is impossible to mitigate every single risk on the supply chains. Due diligence is an ongoing process which has to be improved over time focusing first on the most salient risks before analysing less important risks.

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?

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

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.

Deutsches Aktieninstitut beleives that a certain turnover generated in the EU represents a good link to make third country companies subject to the due diligence obligations, as it shows their significant presence in the EU.

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

In order to treat all companies equally, third country companies doing business in the EU should be subject to the same obligations as EU companies. Enforcement measures could include restrictions on operation within the EU, exclusion from public tenders and others.

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:

We beleive that the EU should use its political weight to include more human rights chapters in free trade agreements with third countries, forcing third country companies to adhere to European standards.

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:

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

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.

We think companies should use these channels to engage with stakeholders, but they should not be required by law to do so.
It is up to the company to put in place a dialogue suited to the size and geographical location with stakeholders and certain mechanism should be proportionate to the relevance of the stakeholder.

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

It should be at the discretion of the company to decide which stakeholder to be represented – based on the size, location, activity.
The EU Commission should be aware that such regulation will lead to pressure to give theoretical reasoning why the state and its authorities should not also be relevant stakeholders in that sense. They do have an interest in the companies. If this were to be intended public bodies would play a two-fold role for companies: as regulators with enforcement powers and private actor whose interests would also have to be taken into

account. This leads to the question of the role of the state as private actor as “stakeholder” in addition to the same issue where it has made us of its regulatory powers: the distinction between public and private law has constitutional status, at least in Germany.

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 | ○ | ○ |
| Other, please specify | ○ | ◉ |

Other, please specify:

It should be up to the company to decide which mechanism is suitable for the stakeholder with which they are engaging – either advisory body, complaint mechanism, etc.

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:

Recently, shareholders have been granted more rights concerning remuneration systems by the SHRD II. Transparency of remuneration systems has also be enhanced. Companies have some time ago started to link elements of the remuneration system to what they report as crucial in their non financial reporting. Due to the Non-Financial-Reporting-Directive companies report relevant information on the policies they implement in relation to environmental protection, social responsibility and treatment of employees, respect for human rights, anti-corruption and bribery, but also diversity on company boards (in terms of age, gender, educational and professional background). As a consequence, remuneration systems proposed to the AGM foresee relevant targets for variable information. Companies have to remain flexible. For example, in a company, for which carbon emission reduction is not a challenge due to the specific situation, the new requirement would be even counter-productive in helping to better incentivise management if there is the need in another area. Another example is holding periods for shares that are incereasingly becoming a standard in remunerations systems in Germany also promoted by the German Corporate Governance Code. This shows that there is no need for further action.  So, the EU-Commission should leave that to the market, where also shareholders are becoming more and more active, as pursued by the EU Commission and as expressed by the SHRD II.

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:

The EU Commission might address soley the supervisory board, here. A supervisory board as a whole must have the knowledge, skills and experience necessary to perform the control function and to assess and supervise the management of the company. This includes expertise on all relevant business areas and accounting. If the supervisory board or its members lack the necessary expertise to be able to assess difficult technical issues with due diligence, the commissioning of a consultant on the basis of a supervisory board or committee resolution is generally permissible. The areas of CSR are manifold. To cover all possibly relevant areas there would numerous experts be neccessary on the board. To elect one expert of one scientific expertise rather doesn't make sense. Therefore, we believe that all board members should take care of the general issues that are reflected in the non-financial reporting, but no single «expert » should be required by regulation.  This should be dealt with by the corporate governance codes that analyse the best practices, if there are any, and include them as a recommendation from which companies can deviate if they state good reasons.

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?

There is already a framework on share buybacks and there are EU market practices which are dealt with by the Market Abuse Regulation. There is immense critisicm by academia on the EY study especially concerning the research on sharebuybacks. Economic scholars inter alia state in their criticism that rather than considering only capital outflows, a more holistic approach would take capital inflows into account as well. For the period 1992-2019, results show no evidence of excessive pay-outs among EU listed

corporations. This is because equity issuance was consistently higher than repurchases and net shareholder pay-outs were about half of total net income and among smaller firms the net shareholder pay-out was negative. Also, three current studies are cited by academia that show that the concern that CEOs use share buybacks to hit earnings per share (EPS) targets in bonus contracts is contradicted by the evidence.

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:

## Section V: Impacts of possible measures

Question 25: Impact of the spelling out of the content of directors' duty of care and of the due diligence duty on the company
Please estimate the impacts of a possible spelling out of the content of directors' duty of care as well as a due diligence duty compared to the current situation. In your understanding and own assessment, to what extent will the impacts/effects increase on a scale from 0-10? In addition, please quantify/estimate in quantitative terms (ideally as percentage of annual revenues) the increase of costs and benefits, if possible, in particular if your company already complies with such possible requirements.

Table

| | 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).

**Contact**

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