

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

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

* 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

* Email (this won't be published)

* Organisation name

255 character(s) maximum

* 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.

* 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

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:

The narrow view, considering only short term profits for the benefit of shareholders, has adversely contributed to the state of our planet - the climate emergency, natural resource depletion. The ongoing demand to manufacture products faster and cheaper which has strong implications for the well-being of workers, communities and customers. This view also risks the future of the next generations. Undoubtedly, the raison d'être of business is to be profitable but this cannot be at the expense of people and the environment. Business can be (and some are) profitable without only considering the bottom line. They are helping people and the society to be more prosperous and attempting to minimise harm to the natural world.

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:

It is hard to argue with the progress made in the last 10 years (since the UNGPs) in how some companies assess and address human rights risks. Leading companies have adopted a formal human rights due diligence policies. In fact, there is some evidence from the Corporate Human Rights Benchmark (2020) that companies which have a HRDD policy 'scored on average four times higher than those companies that did not'. At the same time, according to CHRB 2020, only a minority of companies demonstrate the willingness and commitment to take human rights seriously.' So, though HRDD is an effective tool to advance Human Rights, more companies must do it. Voluntary schemes are not enough to ensure that as proven by the CHRB and other benchmarks. Therefore, what is required is a legal framework which obliges companies to act.

Despite the resistance from some key stakeholders, a legal framework is the appropriate tool. It is worth comparing HRDD to the development of Health and Safety policies in the EU. According to an academic article published in Industrial Health in 2012, health and safety was 'sometimes considered too demanding and over detailed' when the first Directives were passed in 1989. The authors clearly state that 'Their implementation in 27 Member States and the enlargement process have created a beneficial "common acquis" on a modern and advanced policy framework'. It has become a good habit with other business benefits.

(Reference: Occupational Safety and Health in Europe: Lessons from the Past, Challenges and Opportunities for the Future. Diana GAGLIARDI¹, Alessandro MARINACCIO¹, Antonio VALENTI¹ and Sergio IAVICOLI^{1*})

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

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:

According to the ILO 'More than 6 workers among 10 and 4 enterprises among 5 in the world operate in the informal economy'. The people working in those settings tend to be vulnerable to human rights abuses. Though it is not clear to us how a HRDD might impact the informal workers, it is worth raising a concern about the consequences for them.

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

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

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

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| | Relevant | Not relevant | I do not know/I do not take position |
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| 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 | <input checked="" type="radio"/> | <input type="radio"/> | <input type="radio"/> |

the interests of society, please specify:

As mentioned above in Q2, the long term well-being of a company is linked to the well-being of the community and the society it operates in. It is no longer possible to behave as if a company is operating in a vacuum. Companies rely on people, societal arrangements like security, energy, education, transport and on the availability of natural resources. Without society, a company cannot exist.

other interests, please specify:

It is also worth considering future generations as stakeholders because much of the impact of climate change and the environmental degradation will be felt by future generations.

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 |
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| 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 should not be assigned tasks that are associated with democratic institutions like governments. In the UNGPs, it is governments that are obliged to 'respect, protect and fulfil human rights' and companies need to respect human rights.

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:

Without clear and concrete targets, this legislation could create disparities between companies take this seriously and companies which are just doing the bare minimum. In addition, science based targets do lead to reduction in harm as was proven in a recent study which show that firms that had science based targets for emission reduction, actually reduced their emissions in line with Paris. <https://www.businessgreen.com/news/4026241/study-firms-science-targets-slashed-emissions-quarter-paris-agreement>. Upholding human rights is less of a science and more a question of clear commitments (the "tone from the top!"), team management to deliver on those commitments, researching the risks, acting accordingly, monitoring the results, listening to feedback and learning as you go.

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:

A legal obligation is the strongest incentive for directors to overcome their innate tendency to focus on short term financial interests. A duty of care to more than just shareholders would be a very powerful tool to assist directors who do want to balance the interest of all stakeholders but feel that they have no legal grounds to do such a thing. It will also force directors who do not consider it to do it.

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?

1. Companies may decide to operate in different markets;
2. There are some costs, particularly until this process becomes a new habit and while there are also benefits they can't be guaranteed to match month by month, so some companies may suffer to some extent, particularly in the short term.
3. companies might comply with the letter of the law and not with the spirit of it; 4. It is also worth thinking about unintended consequences which may occur – such as adverse impact on the most vulnerable workers (in case companies decide to shorten its supply chain because it is too difficult to implement HRDD on a very long supply chain).

How could these possible risks be mitigated? Please explain.

- *1. The legal framework must be applicable to all companies selling products in the EU;
2. Look for ways to give early adopters who comply with the regulation some sort of financial benefit like lower tax or access to capital (e.g. through the taxonomy process).
3. The framework must be robust enough and have an effective enforcement mechanism
4. There should be periodical reviews to look at the unintended consequences and find a way to remedy those

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

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:

For the HRDD to be taken seriously within a company and for it not to become siloed within the CSR department, it must be part of the mainstream strategy of the company and needs to be discussed and approved at Board level.

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:

We are not in position to answer this question

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:

We are not in position to answer this question

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:

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.

We are not in position to answer this question

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 commend the commission on this definition. We are especially pleased to see the incorporation of climate change and the environment into the definition. Though this definition encompasses most of the important elements of what a good definition of HRDD should include and is based on the UNGPs and the OECD Guidelines, there are a few elements which are, in our opinion missing:
 - * It defines the action that a company needs to take depending on how the company is connected to the

adverse impact but it only mentions causing and contributing. We are concerned that it omits the option that a company is directly linked to an impact. This is a crucial point because in many cases especially down the supply chain, companies are linked to abuses and it is relatively rare to find “causing” or “contributing” by a parent company. The obligation on large companies to use their leverage when they are linked to an adverse impact is a powerful tool. Without ‘linked to’, larger companies could claim innocence and shift the blame towards suppliers.

* We are also concerned that the definition is limited to supply chain and does not look at the full spectrum of the value chain such as the use of products and their impact on HRs.

* The UNGPs emphasise that a company must assess its actual impacts and the potential impact while the above definition does not include the latter (though it refers to foreseeing impacts).

* We believe that there is a need to clarify the supply chain and the subcontractor. In recent comments made by Professor John Ruggie he stated that in his opinion, rather than identifying all tiers, the focus of companies should be on what are the salient human rights risks are for each company regardless if it is in its own operations or somewhere down the supply chain.

* In the same discussion Professor Ruggie also mentioned that a due diligence process must consider the harm caused by business practice such as delayed payment, change of orders etc .

* The UN Guiding Principles are also clear on the need to provide Remedy in the case that you have caused or contributed to the harm and to use leverage to get others to provide remedy in the case where you are only directly linked through business relationships to those causing or contributing to the harm. The focus on remedy for victims is an extremely important part of the UN GPs approach of fixing problems before they become bigger problems if possible.

* And finally, the UNGPs is also expect companies to disclose their process (the risks identified, the plans put in place, the monitoring and the learnings) including to the affected stakeholders as an important part of engaging with them. This disclosure is also very important for investors in the company and those assisting them to fulfil their own responsibilities.

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

- Option 1. “Principles-based approach”: A general due diligence duty based on key process requirements (such as for example identification and assessment of risks, evaluation of the operations and of the supply chain, risk and impact mitigation actions, alert mechanism, evaluation of the effectiveness of measures, grievance mechanism, etc.) should be defined at EU level regarding identification, prevention and mitigation of relevant human rights, social and environmental risks and negative impact. These

should be applicable across all sectors. This could be complemented by EU-level general or sector specific guidance or rules, where necessary

- Option 2. “Minimum process and definitions approach”: The EU should define a minimum set of requirements with regard to the necessary processes (see in option 1) which should be applicable across all sectors. Furthermore, this approach would provide harmonised definitions for example as regards the coverage of adverse impacts that should be the subject of the due diligence obligation and could rely on EU and international human rights conventions, including ILO labour conventions, or other conventions, where relevant. Minimum requirements could be complemented by sector specific guidance or further rules, where necessary.
- Option 3. “Minimum process and definitions approach as presented in Option 2 complemented with further requirements in particular for environmental issues”. This approach would largely encompass what is included in option 2 but would complement it as regards, in particular, environmental issues. It could require alignment with the goals of international treaties and conventions based on the agreement of scientific communities, where relevant and where they exist, on certain key environmental sustainability matters, such as for example the 2050 climate neutrality objective, or the net zero biodiversity loss objective and could reflect also EU goals. Further guidance and sector specific rules could complement the due diligence duty, where necessary.
- Option 4 “Sector-specific approach”: The EU should continue focusing on adopting due diligence requirements for key sectors only.
- Option 5 "Thematic approach": The EU should focus on certain key themes only, such as for example slavery or child labour.
- None of the above, please specify

Please specify:

We would caution against setting some of these approaches against each other. We would suggest taking elements from all options and merging them into an alternative option:

1. Option 3 is preferable to option 2 because the objective is to include the environment;
2. But some aspects of due diligence are by nature principles-based, and others would benefit from clear requirements (and it's always helpful to know the principles behind a requirement, rather than just following a rule);
3. In addition, there are some specific themes (such as conflict, Modern Slavery, or conflict minerals) which merit a specific “thematic” approach, and some sectors which should pay particular attention to particular issues (for example big tech addressing digital rights & their impact on democracy) which it may be

necessary to highlight (either initially, or over time) if the principles or the requirements approach don't result in sufficient attention to the matter.

Considering the different stages of due diligence:

- a. Risk identification: would benefit from minimum process definitions including more guidance on the scope of stakeholder consultation (frequency, coverage, continuity, multi-channel approaches, both "expert" and actually or potentially affected stakeholders or their chosen representatives; feedback to participants etc)
- b. Risk Assessment: intrinsically principles-based [the "salience" of the risk to the victims judged against scale, scope and remediability], though you can (and should) require that the outcome is made public, and communicated back to stakeholders;
- c. Action Plans: you could require that they are made public and consulted upon with relevant stakeholders as minimum procedures, but the idea that they need to be proportionate to the harms you are trying to prevent in an important principle on which to base the exercise, rather than a minimum requirement;
- d. Tracking your success: you can make the frequency of review of your action plans, and disclosure of the review outcomes and further steps taken into minimum procedural requirements, but the important principle on which this is based is that you have to assess whether your action plan is proving adequate to the task (removing or minimising the risk), and if not, determining how to close the gap.

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?

The Corporate Human Rights Benchmark has defined key human rights issues in a number of sectors (extractives, agricultural, apparel, IT manufacturers and automotive) that serve as minimum requirements when assessing companies

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.

Complimentary guidance on stakeholder consultation would be very valuable given the central role of stakeholders in this exercise and the considerable scaling up of current practice envisaged in this regulation. ISO 26000 gives some guidance but a clear statement of good practice based on the experience of the business & human rights community (amongst others) would avoid every company starting with a blank sheet of paper in this important area.

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

- Human rights, including fundamental labour rights and working conditions (such as occupational health and safety, decent wages and working hours)
- Interests of local communities, indigenous peoples' rights, and rights of vulnerable groups

- Climate change mitigation
- Natural capital, including biodiversity loss; land degradation; ecosystems degradation, air, soil and water pollution (including through disposal of chemicals); efficient use of resources and raw materials; hazardous substances and waste
- Other, please specify

Other, please specify:

This list is missing customers as a stakeholder group. It might also be helpful to explicitly include migrants and informal workers as vulnerable groups where working conditions are often worst, and a gender-based analysis of the risks and means of addressing them is normally insightful.

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?

There should be harmonisation with the anticipated SFDR requirements for principal impacts or any differences or additions should be clearly explained. In terms of Human Rights the impacts should include any significant breach of international accepted human rights to align with the UN Guiding Principles on Business and Human Rights

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?

We highlighted above the need for heightened due diligence in relation to conflict, but conflict can also be viewed as a theme meriting specific actions (as the EU has done for conflict minerals). There may be

occasions when specific reporting requirements are merited. The US State Department issued such guidelines in relation to Burma/Myanmar in the past, for example, and the EU created labour reporting standards for companies operating South Africa as part of tackling the international crime of apartheid.

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

SMEs who are also listed companies should be fully included to ensure that investment portfolios are fully covered.

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.

*◆Companies meeting any number-of-employees or turnover threshold that is set for European companies should be subject to the same rules and there should be a turnover threshold for those without a presence in the EU but who sell into the EU in competition with EU companies. This will ensure EU consumers can be reassured that all those selling to them face similar requirements

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

There would need to be a means for companies to meet the reporting requirements if they wish to do so only for their EU based operations or those parts of their enterprise that sold into the EU, and they would need to identify the level of governance that had the necessary authority and role and was responsible for their disclosures. Some might want that to be “below” their global board. It would need to be understood that their global supply chains were still within the scope of the requirements whether those suppliers were third parties or some other part of the global operation.

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:

The best outcome would be global uptake of these standards. Basing them upon globally agreed standards such as the OECD and the UN guiding principles on business and rights will help to facilitate this. In addition the EU should consider what part its trade agreements with third countries can play in globalising these approaches. The EU should also offer “equivalence” arrangements wherever possible to third countries, for example removing the need for additional EU only requirements under this regulation to the extent that their home country adopted equivalent 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:

Where a Company causes or contributes to harm it is reasonable to make them liable for the losses caused to others. But there is a lot more to due diligence than remedy in the form of liability and therefore it would be beneficial to have competent national authorities working to a common standard to monitor and evolve the whole due diligence process.

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:

We monitor court cases for the Corporate Human Rights benchmark and there are some specific problems that could be relevant to the success of this due diligence process.

It has been argued in English courts (by Unilever), that because they did not give detailed advice or guidance to their Kenyan subsidiary at the time of disputed Kenyan elections and because matters were not escalated to London in practice, they could not be held responsible for what took place in the Kenyan plantation. This kind of denial of jurisdiction argument is very unhelpful to the due diligence process and the sharing of expertise within a company.

Another problem in some long-standing cases (for example Dow Chemicals and Bhopal, albeit not a European example) is that once a company has sold its interest in an entity involved in significant human rights or environmental impacts it can also seek to deny legal liability for the events. In that case the remaining toxic waste problems continue to cause environmental and human rights harms long after the original events and without proper cleanup. Some reports claim that more people have died or been injured by the neglect of the cleanup, than the original incident.

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

It should be made clear that a company is responsible (under this due diligence framework) for all its direct and indirect subsidiaries regardless of what business model or management arrangements it chooses to put in place between its operations and head office, and that it does retain oversight responsibilities.

It should also be made clear that selling the relevant interest or terminating the business relationship does not end the due diligence responsibility to do the best one can for the victims, for example, by providing advice and material support that can address ongoing damage arising from past events. Or continuing to press those in a position to provide remedy to the victims to do so, and to assist as appropriate.

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.

It is helpful to use existing channels where they exist, but is also worth observing that they may not avoid be equipped to undertake either human rights or environmental diligence consultations on their own so a proper definition of the necessary consultation for these purposes will be useful.

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

For human rights due diligence consultation should include both experts on the topics/geographies and the actual or potentially affected stakeholders (or their chosen representatives).

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

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:

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:

These are all good ideas when it comes to ensuring that round the board table there is sufficient expertise to make the governance decisions necessary to ensure the right balance of stakeholder and other interests in making business decisions. At least one director needs to have relevant expertise, and, given the complexity of the issues, and the potential challenges of being an isolated director, it will often be necessary to have more than one, particularly in any company facing a number of significant ESG challenges. But this should not substitute for asking these questions when appointing any director and for the board to review its overall competence in the field and reinforce it as necessary as part of the normal process of board review.

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:

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 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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