



INITIATIVE ON SUSTAINABLE CORPORATE GOVERNANCE

Issued 8 February 2021

ICAEW welcomes the opportunity to comment on the consultation published by European Commission on 26 October 2020, a copy of which is available from this [link](#).

ICAEW is listed in the EU Transparency Register (ID number: 7719382720-34). ICAEW has had a presence in Brussels since 1994, providing technical advice across a broad range of EU regulatory matters and facilitating dialogue among stakeholders on key public policy issues. Headquartered in Brussels, the ICAEW Europe Region engages with professional bodies, firms, oversight authorities and market participants across Europe and approximately 5,000 ICAEW members in EU member states outside the UK.

ICAEW supports the intended outcomes for these proposals. However, it is important that the requirements can adapt to the variations which exist between different companies, stakeholder groups and Member States. We suggest that the EU aims for high-level requirements. Allowing discretion for the detailed implementation of requirements will promote proportionality and lead to better outcomes.

Some of the proposals reflect what is already in place in the UK, and the EU may wish to reflect on this experience. UK directors have been subject to a legal duty of care towards stakeholders for well over a decade, but there is dissatisfaction with apparent inability or unwillingness to hold individual directors accountable in appropriate circumstances. Similarly, consultation with stakeholders was one of the additions to the recently revised UK Corporate Governance Code, but a recent [review](#) by the Financial Reporting Council indicates that companies are failing to disclose what happens as a result of this engagement.

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This ICAEW response of 8 February 2021 reflects consultation with the Corporate Governance Committee. The committee is diverse and reflects a wide spectrum of views and specialisms. The investment, non-executive director, charity, academic, audit, legal and proxy adviser communities are represented. The committee informs our thought leadership and policy work on corporate governance issues and related submissions to regulators and other external bodies.

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KEY POINTS

Directors' duty of care-stakeholders' interests

1. It is important to acknowledge that the majority of directors are diligent, and they are often very frustrated by the inability of the authorities to hold negligent directors to account. A realistic prospect of enforcement will encourage all directors to meet or exceed a new legal duty.
2. Although there is usually agreement about the importance of enforcement it is far more difficult to reach a consensus about how to improve. The collective responsibility of boards and confidentiality of decision-making are perceived to be barriers to enforcement. There are also difficult questions around who should take action and how the process will be resourced. The availability of multiple enforcement mechanisms offers a partial solution. Whistleblowing and a complaints mechanism can also be valuable and cost-efficient tools for facilitating enforcement.

Due diligence duty for supply chains

3. The EU's intention to require companies in third countries but operating in the EU to undertake due diligence is a worthwhile ambition. ICAEW has members inside and outside of the EU.

ANSWERS TO SPECIFIC QUESTIONS

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

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

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:

We were initially attracted to the first answer because a holistic approach is needed. However, maximisation of social and environmental is too extreme. These factors need to be balanced with economic/financial performance.

There has been UK legislation in this area for over a decade. Section 172 of the Companies Act (2006) requires directors to 'have regard to' stakeholders' interests while promoting the success of the company for the benefit of its members (shareholders) as whole. This legislation strikes a good balance.

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:

Although a legal framework is needed its success will depend upon proportionality, ie, which companies must comply, and critically, the depth and extent of the due diligence which the companies in scope are required to perform.

The UK's Modern Slavery Act (2015) requires commercial organisations including companies to make a statement about what steps they have taken to ensure that modern slavery is not taking place in their business or supply chain. The organisations which must make these statements are: any organisation in any part of a group structure wherever it is incorporated; which carries on a business (or part of a business) in the UK; supplies goods or services; and has an annual turnover of £36m.

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

One of the concerns with due diligence duties is the particular challenges which SMEs encounter because of their lack of resources. The EU should open a dialogue with SMEs

about what would help them comply. This dialogue will also be a useful opportunity to explore and expand on the benefits which SMEs will enjoy which is an important counterpoint.

Other, please specify:

No reply.

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 (eg, 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:

Proportionality is key to avoiding excessive costs and penalisation of smaller companies with fewer resources including SMEs.

An inevitable consequence of levelling the playing field for compliant companies is that non-compliant companies will be less competitive. This is unavoidable, and it is advantageous if it motivates third country companies to comply.

The EU may wish to consider restricting the EU market to compliant companies. If so it will be important to avoid loopholes, eg, online marketplace retailers must be subject to the due diligence duty.

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

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

	Relevant	Not relevant	I do not know/I do not take a position
The interests of shareholders	x		

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

The interests of society, please specify

All of the listed interests are relevant including the interests of society. It is not enough for private sector companies to be accepted by society. Both will benefit from a shared vision of the future which puts them in lockstep.

other interests, please specify:

No reply.

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 a position
Identification of the company's stakeholders and their interests		x				
Management of the risks for the company in relation to		x				

stakeholders and their interests including on the long run						
Identification of the opportunities arising from promoting stakeholders' interests:					x	

Please explain:

The EU may want to consider the patchwork of existing requirements and cultural variations between Member States, eg, identification of stakeholders and management of associated risks are already either legal obligations or expectations in the UK.

Promoting stakeholders' interests is important as it makes the other two activities of identification and risk management worthwhile. However, we are unclear about what is meant by 'opportunities.' We do not believe there should be a legal obligation to either identify or pursue commercial opportunities.

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 a position

Please explain:

Corporate directors should be required by law to set up adequate procedures. Where relevant they should also set targets which may be quantitative or qualitative or both. However, it is premature to impose science-based targets as legal requirements. One reason for this is that there are differing views about which areas can or should be subject to science-based targets.

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 a position

Please provide an explanation or comment:

Balance is essential because the interests of different stakeholder groups may conflict. The financial success of the company and benefit to members (shareholders) must also be factored in.

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?

Over regulation may discourage entrepreneurial directors, or encourage directors to be too risk averse.

Stakeholder groups change over time.

The duty won't work in practice unless shareholders agree with the duty and support directors when they apply it in their decision-making.

The duty of care may not have the desired outcomes if it is not enforced. Compliant directors may become frustrated by laggards.

How could these possible risks be mitigated? Please explain.

Over regulation can be avoided if an appropriate balance is struck in the duty, see Q1.

Legislation can be drafted flexibly so that new stakeholders are covered.

The EU should seek views from shareholders, including analysing their responses to this consultation. Shareholders may support a duty of care for directors, in fact they may already expect directors to take stakeholders into consideration.

See our comments on enforcement, Q11 -Q13a.

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

Yes. Investors expect the companies in which they invest to identify who their stakeholders are, and which environmental, social and governance (ESG) issues are material to them. Once the material issues have been identified they need to be incorporated in the remuneration framework for directors as appropriate. Failure to manage ESG risks could imperil a company's licence to operate if regulators believe it has abused consumers' trust. Failure to identify ESG opportunities could also threaten the sustainability of the company's business model, eg, demographic changes impact the customer base.

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 a position

Please explain:

Anything less than a holistic approach is very unlikely to be effective. The rebuilding of economies post COVID is an important opportunity to mainstream sustainability which must not be missed.

Enforcement of directors' duty of care

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?

In theory UK law allows shareholders to legally enforce directors' duty of care in their name but on behalf of the company, ie, derivative claims¹. Shareholders can also petition for relief against unfair prejudice². However, difficulties with these methods of direct enforcement have prompted indirect approaches which are also effective.

Investors who monitor for ESG risks and controversies ask companies for explanations about negative events or feedback, and investors will push for action if the response appears inadequate. This may be escalated, eg, through the UK Investment Forum³. In fact the Investment Association has a **public register of negative shareholder votes**. Most negative votes arise from directors' remuneration, and from shareholders' unwillingness to renew directors' membership of company boards.

Although it is difficult to identify cases taken by stakeholders on behalf of the company, foreign direct liability litigation taken by stakeholders on their own behalf, perhaps with the support of a civil society organisation, is more commonplace. A very recent example is a case taken by Friends of the Earth Netherlands (Milieudefensie) and four Nigerian farmers who **successfully sued** Royal Dutch Shell in the Dutch Court of Appeal for an incident which occurred in Nigeria which was caused by Shell Nigeria.

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?

No reply.

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 a position

Please explain your answer:

¹ Part 11 of the Companies Act (2006).

² Companies Act (2006), s.994.

³ **The Investment Forum's 2020 review** has some examples through its Stewardship 360 programme, see pages 37 & 38.

Although stakeholders should be able to take a role in enforcement there must not be complete reliance on them to initiate and pursue enforcement of directors' duty of care.

Stakeholders can only be effective if they have sufficient information about what to do if they suspect a breach. For example, they need to know how to make a complaint to a competent national authority. There also needs to be greater awareness of the ability of stakeholders to submit specific instance complaints about breaches of the OECD Guidelines for Multinational Enterprises to National Contact Points.

Stakeholders can play an important role as whistleblowers if they know what to do and when to do it, and if they receive sufficient reassurance about the process, eg, whistleblowers should have a choice about whether to blow the whistle anonymously or go on-the-record.

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.

In theory all stakeholder groups can play a role. However, stakeholder groups vary in terms of their cohesion and the strength of their connection with the company, and this influences the role they can and should play in enforcement of the duty of care.

For example, employees have a uniquely close connection with companies and they may even be organised under the umbrella of unions. By contrast, local communities are more likely to play the role of an interested party than an active participant unless they have the support of a civil society organisation.

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.

Yes and no. The acknowledgment that due diligence is inherently risk-based, proportionate and context specific is welcomed. We agree that the extent of implementing actions should depend on the risks of adverse impacts the company is possibly causing, contributing to or should foresee.

Companies should have 'adequate processes' to prevent risks arising in their own operations. However, the processes for supply chains cannot be as comprehensive as some chains will extend beyond the EU. Companies should comply with the due diligence requirement for supply chains if they make 'reasonable efforts' ie, this terminology should not be limited to the duty on companies to identify suppliers and subcontractors.

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, ie, 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:

No reply.

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?

No reply.

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.

A sectorial approach is insufficient, and therefore a horizontal approach is needed. Option 3 is the best choice for legal certainty because it combines a minimum set of requirements for the necessary processes with further guidance and sector specific rules.

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

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

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

Climate change mitigation

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

Other, please specify

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

No reply.

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?

What's important is that the requirements are certain and achieve the right outcomes, not whether they are set by the EU or by another international body, eg, the UN global compact is pertinent to human rights and the International Labour Organization opines on labour rights.

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

No reply.

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

No reply.

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).

All SMEs should be excluded

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

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

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

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

SMEs should have lighter reporting requirements.

Capacity building support, including funding

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

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

Other option, please specify

SMEs should also be allowed longer to implement the new requirements.

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.

No reply.

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

Ideally the obligations will be exactly the same for third country companies and EU companies as this is the only approach which will create a truly level playing field. Third country companies should only be allowed to tender for contracts with EU member state governments if they adhere to EU standards.

The UK's Modern Slavery Act (2015) is a precedent for this. It has extraterritorial effect because it applies to overseas companies which do business in the UK, see Q2.

Question 18: Should the EU due diligence duty be accompanied by other measures to foster more level playing field between EU and third country companies?

Yes

No

I do not know

Please explain:

Question 19: Enforcement of the due diligence duty

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:

The availability of all three mechanisms is optimum, This will allow proportionate enforcement, with judicial enforcement reserved for the most egregious cases. Research shows that the judiciary are prepared to question directors' decision-making⁴.

Supervision based on complaints is important because it will allow stakeholders to raise concerns about suspected breaches of the due diligence duty.

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

No reply.

⁴ **Business Judgment and the Courts** by University of Leeds Law School, University of Liverpool Management School and Liverpool John Moores University School of Law..

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

No reply.

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

No reply.

Section IV: Other elements of sustainable corporate governance

Question 20: Stakeholder engagement

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.

The full extent of what's required for employees by EU law may not be appropriate for all stakeholder groups. Taken as a whole, the information and consultation requirements for employees, European Works Councils and compulsory employee representation on supervisory boards could be too onerous to replicate for all stakeholder groups.

It would be better if companies need to agree what will work for different stakeholder groups in consultation with the groups themselves, eg, there should be flexibility as to whether companies engage with different stakeholder groups separately or combine groups. All parties should be conscious that whatever is created must be sustained when key individuals are no longer available or if initial enthusiasm wanes. The approach needs to be robust and formal enough to withstand stresses caused by any disagreement between the company and stakeholders, or between stakeholders.

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

As a minimum: employees, suppliers, customers, community and the environment.

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 may be better not to promote any particular mechanism, but the EU could be a conduit for the sharing of non-compulsory best practice.

Stakeholder groups with a looser connection to a company may prefer a digital approach, eg, some of the community may find it difficult to belong to a body or attend meetings and in these circumstances a digital platform may be a good solution.

Question 21: Remuneration of directors

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) **:7 stars**

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:

Simplicity is preferable as all other approaches can be manipulated to a greater or lesser extent. The EU may like to bear in mind that non-financial measures are more likely to pay out than financial measures, as many are defined in qualitative rather than quantitative terms. Having said this, Germany has required companies to incorporate ESG criteria in remuneration policies in its implementation of second shareholder rights directive.

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.

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:

Nominations committees need complete flexibility as their recruitment decisions must reflect the company's priorities. A minimum number or percentage of specialist directors in the areas mentioned would be out of step with the lack of equivalent requirements for gender or ethnic diversity.

Question 23: Share buybacks

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

In your view, should the EU take further action in this area?

I strongly agree

I agree to some extent

I disagree to some extent

I strongly disagree

I do not know

I do not take position

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

Any further action by the EU would need to be evidenced and we are aware of the following research in the UK:

1. **Research by the Trades Union Congress and High Pay Centre found that:**
 - Across the FTSE 100 as a whole, returns to shareholders increased by 56% (despite net incomes falling by 3% over the period). This resulted from a 45% increase in dividends, while share buybacks more than doubled.
 - While FTSE 100 returns to shareholders rose by 56% the median wage for UK workers increased by 8.8%.
 - In 27% of cases returns to shareholders were higher than the company's net profit, including 7% of cases where dividends and/or buybacks were paid despite the company making a loss. In 2015 and 2016, total returns to shareholder came to more than total net profits for the FTSE 100 as a whole.
2. **Research into share buybacks by the Department of Business, Energy and Industrial Strategy** did not establish that businesses purchase their own shares as a means to inflate corporate earnings or increase executive pay.

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

COVID-19 has underlined the importance of all stakeholders but particularly employees. Some Member States require companies to have an employee director. The value of employee directors has been formally acknowledged for the first time in the UK in the revised Corporate Governance Code.⁵ ICAEW has developed its thinking about **how employee directors add value**. However, a recent **review by the Financial Reporting Council** shows that only 0.6% of companies have chosen the workforce director option for their engagement with this key stakeholder group

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.

⁵ Provision 5.

No reply.

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).

No reply.