Sustainability Concept in Company Law and Corporate Governance: Why, How and Who

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The aim of this chapter of the book is to offer a contribution to a heated debate topic on the potential of company law through corporate governance framework to better support a sustainable development. In the overall picture of different regulatory approaches and techniques and with the focus on the ongoing developments at the EU company law, hard law legislative solutions concerning corporate purpose and director's duty of care as well as mandatory due diligence that are at the core of sustainable corporate governance, as those enabling to promote positive contributions by the companies to sustainable development and tackling adverse impacts on society associated with their operations, are addressed.

Keywords: Sustainability; sustainable development; United Nations 2030 Agenda for Sustainable Development Goals; company law; EU company law; corporate governance; corporate sustainability; mandatory due diligence

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1. Introduction

Lively discussions on sustainability in company law and thus the role of the companies have been going on during the last years. They form part of the broader debate over the regulatory approaches on whether and how to incorporate or reflect sustainability in various fields of laws. In that context it is worth mentioning that the EU and its 27 Member States are committed to the 2030 Agenda for Sustainable Development of the United Nations and its implementation, adopted by all United Nations Member States[2].

The 2030 Agenda includes the 17 Sustainable Development Goals and their related 169 targets and it provides a new policy framework aimed to balance three dimensions – economic, social and environmental (profit, people and planet) and to ensure that no one is left behind[3].

Sustainable development of Europe is embodied in the Treaty on European Union[4], and the UN Sustainable Development Goals are in line with the European vision[5].

There is, however, a different progress in achieving UN Sustainable Development Goals among the Member States, and it can be challenging to attain them by 2030[6]. In searching the ways on how to accelerate the sustainable transition, a role of the companies in contributing towards

[2] Available at: http://www.un.org.cn/info/6/620.html ; https://www.un.org/en/about-us .

[3] General Assembly of United Nations, *Transforming our world: the 2030 Agenda for Sustainable Development, Resolution*, 2015, available at: https://www.un.org/ga/search/view_doc.asp?symbol=A/RES/70/1&Lang=E .

[4] See Article 3, paragraphs 3 and 5, of the Treaty on European Union (consolidated version), available at: http://data.europa.eu/eli/treaty/teu_2016/2020-03-01 .

[5] For the policy commitment at the EU level, see: B. Sjåfjell, *Sustainable Value Creation Within Planetary Boundaries - Reforming Corporate Purpose and Duties of the Corporate Board* (August 3, 2020), «Sustainability», vol. 12.15 (2020), 6245; «University of Oslo Faculty of Law Research Paper», No. 2020-20; «Nordic & European Company Law Working Paper», No. 21-04, available at: «SSRN», https://ssrn.com/abstract=3666952, p. 2; see also: European Commission, *Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions, Next steps for a sustainable European future, European action for sustainability*, 2016, COM/2016/0739 final.

[6] Sustainable Development Solutions Network and Institute for European Environmental Policy, *Europe Sustainable Development Report 2021*, available at: https://eu-dashboards.sdgindex.org , pp. vii, 7-8, 11, 15. The same holds true in achieving the objectives of the Paris Climate Agreement of 2015 (which together with the UN Sustainable Development Goals viewed as a package) oriented towards climate-neutrality by 2050.

sustainable development has been emphasized[7] by better integrating sustainability into the corporate governance framework[8].

Having this in mind, the aim of the chapter of the book is to deliver to a heated debate topic on the potential of Company law through corporate governance framework to better contribute to the sustainable development. In the overall picture of different regulatory approaches and techniques and with the focus on the ongoing developments at the EU Company law, hard law legislative solutions concerning corporate purpose and director's duty of care as well as mandatory due diligence that are at the core of sustainable corporate governance are addressed.

2. Why: potentials for Company law to contribute to a better sustainable development

Companies have done much in voluntary pursuing responsible business conduct initiatives[9]. International soft law instruments are helpful for business in determining guidelines for responsible business conduct standards, for example, the UN Guiding Principles on Business and Human Rights[10], OECD Guidelines for Multinational Enterprises[11] and complementary OECD due diligence guidance for responsible business conduct[12], Tripartite Declaration of Principles concerning Multinational Enterprises and Social Policy of the International Labour

[7] European Commission, *Reflection paper - Towards a Sustainable Europe by 2030*, Brussels 30.1.2019, COM (1019) 22 final, pp. 26-27.

[8] European Commission, *Communication from the Commission to the European Parliament, the European Council, the Council, the European Economic and Social Committee and the Committee of the Regions on the European Green Deal*, Brussels, 11.12.2019, COM(2019) 640 final, p. 17; European Commission, *Communication from the Commission to the European Parliament, the European Council, the Council, the European Economic and Social Committee and the Committee of the Regions Europe's moment on the Repair and Prepare for the Next Generation*, Brussels, 2020, COM(2020) 456 final, p. 6.

[9] See, *e.g.*, European Commission, *Reflection paper - Towards a Sustainable Europe by 2030*, cit., pp. 33-35.

[10] UN, *Guiding Principles on Business and Human Rights*, 2011, available at: https://www.ohchr.org/Documents/Publications/GuidingPrinciplesBusinessHR_EN.pdf.

[11] OECD, *OECD Guidelines for Multinational Enterprises*, OECD Publishing, Paris, 2011, available at: http://dx.doi.org/10.1787/9789264115415-en.

[12] OECD (2018), *OECD Due Diligence Guidance for Responsible Business Conduct*, available at: https://www.oecd.org/investment/due-diligence-guidance-for-responsible-business-conduct.htm. For sector-specific guidance on due diligence for responsible business conduct, see: https://mneguidelines.oecd.org/sectors/.

Organization[13], G20/OECD Principles of Corporate Governance with the focus on public companies[14], as well as other voluntary initiatives promoting corporate sustainability, such as the UN Global Compact[15].

There is, however, ongoing debate about the sufficiency of a voluntary soft-law approach and permissive regulations and hence a potential for hard law in the field of company law to contribute in accelerating the progress of achievement of the UN Sustainable Development Goals. In particular, the EY study on directors' duties and sustainable corporate governance prepared for the European Commission in 2020, gave a stimulus for developing the heavy discourse. For example, according to the EY study, a tendency for the EU listed companies is "to focus on short-term benefits of shareholders rather than on the long-term interests of the company", and failure "to capture the full extent of long-term sustainability risks and impacts"; claiming that the *status quo* falls short in achieving the UN Sustainable Development Goals[16].

The EY study hence argues for the potential EU legislative intervention[17].

Another study on due diligence requirements through the supply chain prepared by BIICL, Civic Consulting and LSE Consulting of the same year, commissioned by the European Commission, has focused on due diligence processes to address the adverse human rights and environmental impacts in companies' own operations and in their supply chain. The study has revealed that one-third of business respondents confirmed they performed due diligence which takes into account all human rights and environmental impacts, and another one-third – a due diligence to a limited extent[18]. Alongside with the sector-specific

[13] International Labour Organization, *Tripartite Declaration of Principles concerning Multinational Enterprises and Social Policy*, 1977 (with its further amendments of 2000, 2006, 2017), available at: https://www.ilo.org/manila/publications/WCMS_647984/lang--en/index.htm.

[14] OECD, G20/OECD Principles of Corporate Governance, OECD Publishing, Paris, 2015, available at: http://dx.doi.org/10.1787/9789264236882-en.

[15] Available at: https://www.unglobalcompact.org/what-is-gc/mission/principles.

[16] European Commission, Directorate-General for Justice and Consumers, *Study on directors' duties and sustainable corporate governance: final report*, Publications Office, Brussels, 2020 *https://data.europa.eu/doi/10.2838/472901* (hereinafter, "EY study"), p. vi.

[17] *Ibidem*, pp. vi-xii.

[18] European Commission, Directorate-General for Justice and Consumers, F. Torres-Cortés, C. Salinier, H. Deringer, *et Alii*, *Study on due diligence requirements through the supply chain: final report*, Publications Office, Brussels, January 2020, available at: https://data.europa.eu/doi/10.2838/39830 (hereinafter: "BIICL, *Civic Consulting and LSE*

initiatives already undertaken at the EU level, the BIICL, Civic Consulting and LSE Consulting study suggests further considering the possible regulatory options (both soft law– and hard law– approaches as well as smart mix); and a harmonized general mandatory due diligence requirement for adverse human rights and environmental impacts, as a legal duty or standard of care, to be applied horizontally across sectors at the EU level is a possible solution[19].

With the view that companies could take on a bigger role in contributing into the overall progress to achieve the UN Sustainable Development Goals[20], and taking into account the Covid-19 pandemic related-developments that witness increased debate on corporate sustainability, there are ongoing discussions over corporate governance framework being more aligned towards sustainability objectives. The traditional approach[21] claiming that other areas of law more effectively deal with the problematic issues associated with that particular field (tax, labour, environmental, etc.) is also being contested by arguing for a coherent approach in a policy lawmaking[22]. There are, however, divergent views as both to the regulatory approaches and techniques to be dealt with in achieving the policy goals and their effects.

Consulting Study"), p. 16.

[19] BIICL, *Civic Consulting and LSE Consulting Study*, cit., pp.15-23 and pp. 231-260.

[20] *Europe Sustainable Development Report 2021*, cit., pp. 52-53; Sustainable Development Solutions Network and Institute for European Environmental Policy, *Europe Sustainable Development Report 2020*, available at: *https://www.sdgindex.org/reports/europe-sustainable-development-report-2020/*, p. 63.

[21] See, *e.g.*: E.B. Rock, *For Whom is the Corporation Managed in 2020?: The Debate over Corporate Purpose* (May 1, 2020), «European Corporate Governance Institute - Law Working Paper», No. 515/2020; «NYU School of Law, Public Law Research Paper», No. 20-16, and «NYU Law and Economics Research Paper», available at «SSRN»: https://ssrn.com/abstract=3589951, p. 5 and p. 25; M.J. Roe, H. Spamann, J.M. Fried, C.C. Y. Wang, *The European Commission's Sustainable Corporate Governance Report: A Critique* (October 14, 2020), «European Corporate Governance Institute - Law Working Paper», No. 553/2020 and «Harvard Public Law Working Paper», No. 20-30», and «Yale Journal on Regulation Bulletin», available at «SSRN»: https://ssrn.com/abstract=3711652, pp. 149-150; *e.g.*, tax law.

[22] B. Sjåfjell, *Reforming EU Company Law to Secure the Future of European Business* (March 4, 2021), in *University of Oslo Faculty of Law Research Paper*, No. 2021-05 (Preprint of article in *European Company and Financial Law Review*, 2/2021); in *Nordic & European Company Law Working Paper*, No. 21-13, available at: *https://ssrn.com/abstract=3797685*, 2 and 15; *Europe Sustainable Development Report 2021*, cit., x.

3. How and who: solutions for a more sustainable corporate governance framework

It is widely acknowledged that transparency rules implemented through corporate sustainability reporting should be perceived as added value thereto. Indeed, pursuant to the EU Company law, accounting reporting for large public-interest companies requires to disclose sustainability-related matters[23]. And currently, there is the EU legislative initiative under way aiming to improve corporate sustainability reporting itself, as well as to broaden the scope of the reporting companies[24].

Nevertheless, there is much less consensus on whether, in addition to the improved disclosure requirements, and in coordination with them, mandatory substantive rules in the area of corporate governance framework should also be enacted; and, if so, what legal instruments – national or European – embedding those rules are to be deemed the most appropriate.

The question as to whether and how the corporate governance framework could be better adapted to achieve a greater sustainability calls for the need to consider a number of legal tools and to evaluate them carefully (for example: (re)definition of corporate purpose taking into account broader interests, expanding and/or clarifying directors' duties in relation to sustainability, incorporating sustainability expertise at the level of the board and greater diversity on boards, better linking directors' remuneration to sustainability targets[25], putting in place loyalty shares, revisiting enforcement tools, establishing mandatory due diligence, etc.).

[23] Article 19a of Directive no. 2013/34/EU of the European Parliament and of the Council of 26 June 2013 on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings, amending Directive no. 2006/43/EC of the European Parliament and of the Council and repealing Council Directives 78/660/EEC and 83/349/EEC, available at: *http://data.europa.eu/eli/dir/2013/34/2021-12-21*. Large public-interest companies with more than 500 employees have to include in the management report a non-financial statement containing environmental, social and employee matters, respect for human rights, anti-corruption and bribery matters, *inter alia* reporting on due diligence.

[24] EU Commission, *Proposal for a Directive of the European Parliament and of the Council amending Directive 2013/34/EU, Directive no. 2004/109/EC, Directive no. 2006/43/EC and Regulation (EU) no. 537/2014, as regards corporate sustainability reporting*, COM(2021)189 final, 2021/0104(COD). For more information, see: https://ec.europa.eu/info/publications/210421-sustainable-finance-communication_en#csrd.

[25] Articles 9a and 9b of the Directive no. 2007/36/EC of the European Parliament and of the Council of 11 July 2007 on the exercise of certain rights of shareholders in listed companies (consolidated text), available at: *http://data.europa.eu/eli/dir/2007/36/2017-06-09*.

There are pros and cons arguments in relation to each of the various legal tools, either in isolation or in combination, for Company law to pursue the policy goals that could produce desirable changes.

Although there are divergent views as to the most appropriate solutions, those enabling to promote positive contributions by the companies to sustainable development and tackling adverse impacts on society associated with corporate operations, have to be addressed. In that vein, corporate purpose and director's duty of care, as well as mandatory due diligence may be deemed at the core of sustainable corporate governance, thus deserving some further considerations.

3.1. Corporate purpose and director's duty of care

A corporate purpose as the central concept in corporate governance attracted considerable attention from scholars. The two prevailing theories defining a corporate purpose, *i.e.* the shareholder primacy theory aimed to promote shareholder value (and the enlightened shareholder value approach when stakeholder interests are considered as long as it is in the interest of shareholders, as the shareholder primacy doctrine) and the stakeholder theory focusing on pluralistic governance model[26], embodied either as a hard law rule or a social norm, design boundaries for corporate directors in directing and controlling the companies. The corporate purpose helps to define what duties company's directors have.

Sustainable corporate governance brought a renewed emphasis on the pluralistic governance model, balancing various stakeholders' interests. Corporate business practices that integrate economic, social, and

[26] More about the doctrines with the related references, see: L.A. Bebchuk, R. Tallarita, *Will Corporations Deliver Value to All Stakeholders?* (August 4, 2021), «Vanderbilt Law Review», vol. 75 (May, 2022), available at «SSRN»: https://ssrn.com/abstract=3899421 , p. 1, pp. 10-13, pp. 22-23, and p. 52; H. Fleischer, *Corporate Purpose: A Management Concept and its Implications for Company Law* (January 21, 2021), «European Corporate Governance Institute - Law Working Paper» No. 561/2021, available at «SSRN»: https://ssrn.com/abstract=3770656; G. Ferrarini, *Corporate Purpose and Sustainability* (December 7, 2020), «European Corporate Governance Institute - Law Working Paper» No. 559/2020, available at «SSRN»: https://ssrn.com/abstract=3753594 (an edited version of this paper appears as a chapter in D. Busch, G. Ferrarini, S. Grünewald (Eds.), *Sustainable Finance in Europe - Corporate Governance, Financial Stability and Financial Markets*, Palgrave-MacMillan-Springer, Cham (CH) 2021, pp. 85-160); M. Petrin, *Beyond Shareholder Value: Exploring Justifications for a Broader Corporate Purpose* (November 1, 2020), available at «SSRN»: https://ssrn.com/abstract=3722836, and also in E. Pollman, R.B. Thompson (Eds.), *Research Handbook on Corporate Purpose and Personhood*, Edward Elgar Publishing, Chalthenam 2022, pp. 345-362.

environmental issues (all three together being dimensions of sustainability) are essential in achieving more sustainable development[27]. Companies are to be encouraged to focus on long-term and sustainable performance[28]. In that context, one could argue that a corporate purpose as a core concept of corporate governance should reflect a broader view of stakeholders' interests. In its own turn, the corporate purpose-related discussions in the context of sustainability may involve a debate over whether a company has to simultaneously generate social value alongside profit, and which essentially points to even more fundamental question on the role of the companies in the contemporary society[29].

Sustainability objectives should not be, however, viewed in contravention of the overall purpose of the company as a commercial enterprise and an investment vehicle for the shareholders. Concept of sustainability does not in itself modify traditional understanding of the company to be it a fundamentally different legal entity, *e.g.* a non-profit entity, or a social enterprise aimed to pursue social goals and solve social problems[30]. Sus-

[27] European Commission, *European action for sustainability*, cit., 1-2 and 17; B. Sjåfjell, *Sustainable Value Creation*, cit., 5; C.L. Villiers, B. Sjåfjell, G. Tsagas, *Stimulating Value Creation in a Europe in Crisis* (January 7, 2022), «University of Oslo Faculty of Law Research Paper» No. 2022-01, pp. 4-9, available at «SSRN»: https://ssrn.com/abstract=4003345 , and also in B. Sjåfjell, G. Tsagas, C. Villiers (Eds.), *Sustainable Value Creation in the EU: Towards Pathways to a Sustainable Future through Crises*, Cambridge Univ. Press, Cambridge 2022 (Chapter 1).

[28] See European Commission, *The European Green Deal*, cit., p. 17; see also *sub* Action 10, in European Commission, *Communication from the Commission to the European Parliament, the European Council, the Council, the European Central Bank, the European Economic and Social Committee and the Committee of the Regions, Action Plan: Financing Sustainable Growth*, 2018, COM/2018/097 final, p. 3 and p. 11.

[29] H. Fleischer, *Corporate Purpose: A Management Concept and its Implications for Company Law,* cit. pp. 13 ff.; E.B. Rock, *For Whom is the Corporation Managed in 2020?: The Debate over Corporate Purpose*, cit., p. 6 and p. 30; J. Quinn, *The Sustainable Corporate Objective: Rethinking Directors' Duties*, «*Sustainability*», vol. 11.23 (2019), p. 6734, available at: https://doi.org/10.3390/su11236734 , p. 2; C. Mayer, *The Governance of Corporate Purpose* (May 12, 2021), «European Corporate Governance Institute - Law Working Paper» No. 609/2021, available at «SSRN»: https://ssrn.com/abstract=3928613 , pp. 1-20 (stating that corporate purpose is about producing profitable solutions, not profiting from producing problems as well as avoiding detriments to others).

[30] As to a re-definition of the purpose of the company as being "to create sustainable value within planetary boundaries", without a fundamental change of the nature of the company, see B. Sjåfjell, *Reforming EU Company Law*, cit., pp. 16-17; B. Sjåfjell, *Sustainable Value Creation*, cit., 6. As to "social enterprises", see: Article 2, paragraph 1) and paragraph 13) of the Regulation (EU) No. 2021/1057 of the European Parliament and of the Council of 24 June 2021, establishing the European Social Fund Plus (ESF+) and repealing Regulation (EU) No. 1296/2013, available at: http://data.europa.eu/eli/reg/2021/1057/2021-06-30;

tainability is predominantly about the way (manner) in how the company pursues its corporate purpose. The duty of care of directors should thus reflect undertaking towards sustainability.

It has been suggested that replacement of the shareholder primacy model with the stakeholder governance model does not necessarily ensure producing expected effects in properly addressing stakeholders' interests[31]. As responsible business conduct and new business models are considered horizontal enablers for sustainable transition[32], rather than revisiting the concept of a corporate purpose, a debate over the directors' mandate directing the company in a more sustainable way (manner) could proceed.

Corporate directors are the key players to ensure company's strategies, business models and business practices to be aligned with the sustainability objectives. At the company setting, the boards are in the best position to further develop responsible companies[33]. One could view this with the similar pattern emerging in Corporate Governance Codes[34] orienting the boards to direct the companies towards the long-term success and sustainable value creation of the enterprise[35]. Although open-ended aspects of sustainable business standards may possess a difficulty in shaping their contours by directors and finding equilibrium in address-

European Commission, *Social enterprises and their ecosystems in Europe - Comparative Synthesis Report* (drafted by C. Borzaga, G. Galera, B. Franchini, S. Chiomento, R. Nogales, C. Carini), Publications Office of the European Union, Luxembourg, 2020, available at: https://europa.eu/!Qq64ny.

[31] L.A. Bebchuk, R. Tallarita, *Will Corporations Deliver Value to All Stakeholders?*, cit. (showing empirical findings of the review of corporate governance documents of more than one hundred US public companies those joined the Business Roundtable's 2019 Statement on the Purpose of a Corporation committing to deliver value to all stakeholders suggest that the companies retain shareholder primacy).

[32] European Commission, *Reflection paper*, cit., p. 14, and pp. 26-27.

[33] R.G. Eccles, M. Johnstone, Louis, C. Mayer, J.C. Stroehle, *The Board's Role in Sustainability*, «Harvard Business Review» (September-October 2020), available at: https://hbr.org/2020/09/the-boards-role-in-sustainability .

[34] G. Ferrarini, M. Siri, S. Zhu, *The EU Sustainable Governance Consultation and the Missing Link to Soft Law* (April 9, 2021), «European Corporate Governance Institute - Law Working Paper» No. 576/2021, available at «SSRN»: https://ssrn.com/abstract=3823186, pp. 10-11; H. Fleischer, *Corporate Purpose: A Management Concept and its Implications for Company Law*, cit., pp. 16-18 (with specific reference to the German Corporate Governance Code).

[35] Also see B. Sjåfjell, *Sustainable Value Creation*, cit., pp. 4-7 (suggesting to implement a duty of the board to promote sustainable value creation within planetary boundaries to have the corporate purpose determined and thus operating as sustainable value creation within planetary boundaries).

ing sustainability elements is a challenging task, business judgment rule should guide directors in business decision making.

In that context it should be mentioned that in 2020, the European Commission published the sustainable corporate governance initiative to improve the EU regulatory framework on company law and corporate governance by enabling companies to focus on long-term sustainable value creation, as a complementary to the review of the Non-Financial Reporting Directive[36]. According to the summary feedback of the subsequently launched public consultation by the European Commission, the respondents in general supported a holistic approach to be integrated into corporate decision making[37].

It is, however, worth noting that the EY study, which was the basis for the initiative of the European Commission in relation to "directors' duty of care – stakeholder interests", has been met with the heavy criticism due to the various reasons – methodology, research evidences and reform proposals[38]. Others submit that the criticism against the EY study should not distract the main emphasis that, in the context of global challenges such as climate change, the company law has potential to promote sustainability at the EU level, albeit a nudging regulatory approach should be used instead, *i.e.*, a mix of soft law combined with mandatory procedural

[36] European Commission, *Inception Impact Assessment on sustainable corporate governance*, Ref. Ares(2020)4034032 - 30/07/2020, available at: https://ec.europa.eu/info/law/better-regulation/have-your-say/initiatives/12548-Sustainable-corporate-governance_en.

[37] European Commission, Directorate-General Justice and Consumers, *Summary report – public consultation on sustainable corporate governance initiative* (26 October 2020 – 8 February 2021), available at: https://ec.europa.eu/info/law/better-regulation/have-your-say/initiatives/12548-Sustainable-corporate-governance/public-consultation_en, pp. 4-6.

[38] See, *e.g.*, M.J. Roe, H. Spamann, J.M. Fried, C.C.Y. Wang, *The European Commission's Sustainable Corporate Governance Report: A Critique*, cit.; A. Edmans, *Response to the EU Commission Study on Sustainable Corporate Governance*, London Business School European-Commission-Sustainable-Corporate-Governance.pdf, 2020, available at: www.alexedmans.com; K. Lannoo, J. Lau Hansen, A. Thomadakis, *Are European listed corporations short-termist?*, in *European Capital Markets Institute Commentary*, No. 71 (January 2021), available at: https://www.ecmi.eu/sites/default/files/are_european_listed_corporations_short_termist.pdf; European Company Law Experts Group, *Comment on the European Commission's Consultation Document: Proposal for an Initiative on Sustainable Corporate Governance*, 2020, available at: https://europeancompanylawexperts.wordpress.com/publications/comment-by-the-european-company-law-experts-group-on-the-europeancommissions-consultation-document-proposal-for-an-initiative-on-sustainable-corporate-governance/; see also, G. Ferrarini, M. Siri, S. Zhu, *The EU Sustainable Governance Consultation and the Missing Link to Soft Law*, cit., pp. 7-8.

rules[39]. In the similar vein, some suggested sustainability disclosure, soft law instruments and directors' incentives aligned with sustainability targets as preferred solutions rather than reforming substantive directors' duties at the EU level[40]. The subsidiarity principle seems to be among the issues that raise significant concerns about the potential harmonization efforts[41]. On the other hand, given the overreaching EU policy objective for sustainable development, there is a support for a harmonized duty requiring company's directors to promote sustainable value creation as reflecting the company's role in a modern society while highlighting that sustainability objectives cannot be sufficiently achieved at the national level[42]. Some stresses the key role and potential of the private sector in sustainable transformation and thus, alongside with the due diligence requirement, the need at the EU level to clarify directors' duties in relation to strategic oversight of sustainability matters and to align incentives for executives with the sustainability targets[43]. As a compromise, it has been also suggested to focus on long-term value creation and on sustainable corporate governance, albeit contesting the EY study and recommending carrying out further analysis on the effects of different corporate governance mechanisms and on possible, alternative regulatory instruments[44]. Current academic literature generally submits that sufficiently weak en-

[39] F. Möslein, K.E. Sørensen, *Sustainable Corporate Governance: A Way Forward* (January 4, 2021), «European Corporate Governance Institute - Law Working Paper» No. 583/2021, available at: https://ssrn.com/abstract=3761711; in *European Company Law Journal*, no. 1 (2021), pp. 7-14.

[40] See, *e.g.*, G. Ferrarini, M. Siri, S. Zhu, *op. cit.*, p. 7, and M.J. Roe, H. Spamann, J.M. Fried, C.C.Y. Wang, *op. cit.*, p. 150 (supporting the idea of aligning directors' private incentives with social goals in the pay scheme).

[41] See, G. Ferrarini, *Corporate Purpose*, cit., p. 61, and M.J. Roe, H. Spamann, J.M. Fried, C.C.Y. Wang, *The European Commission's Sustainable Corporate Governance Report: A Critique*, cit., p. 134, p. 138.

[42] See, B. Sjåfjell, *Reforming EU Company Law*, cit., pp. 3-6 (with regard to the EU legal basis for sustainability reforms), B. Sjåfjell, *Sustainable Value Creation*, cit., pp. 10-11, and J. Quinn, *The Sustainable Corporate Objective: Rethinking Directors' Duties*, cit., p. 9.

[43] See, *Open letter: An encompassing approach to effective Sustainable Corporate Governance to European Commission President Ursula von der Leyen and Vice-President Věra Jourová from WWF European Policy Office, Finance Watch, Share Action, Frank Bold, Economy for the Common Good*, Oxfam, 31 January 2022, available at: https://www.finance-watch.org/publication/joint-statement-ngos-express-deep-concerns-on-the-upcoming-sustainable-corporate-governance-initiative/.

[44] See A. Bassen, K. Lopatta, W.G. Ringe, *Feedback from University of Hamburg*, 2020, available at: https://ec.europa.eu/info/law/better-regulation/have-your-say/initiatives/12548-Sustainable-corporate-governance/F594615_en.

forcement of directors' duties in Member States may result in not achieving the effect intended from the reform[45].

The intensive legal policy discourse regarding sustainability in corporate governance is not yet over and, at the European level, the way forward remains to be seen.

3.2. Mandatory due diligence

Another fundamental issue in company law relates to corporate externalities that harm society[46]. It has been argued that voluntary soft-law approach alone and disclosure requirements are not sufficient to encourage companies to better internalize externalities generated by their operations[47]. In that respect, alongside with the transparency rules for corporate sustainability reporting, a mandatory due diligence requirement for the company, as a preventive measure and a substantive corporate duty (standard of care) premised on not-to-harm basis, could be an appropriate legal technique to consider.

The due diligence concept is aimed to deal with the externalities associated with the company's operations by establishing and implementing processes, an integral part of the corporate decision-making and risk management, aimed to identify, prevent, mitigate and account for severe impacts, such as human rights and environmental, both in the company's own operations and in its supply chain or value chain[48]. Under the due diligence concept, companies need not only to follow responsible business conduct standards in their own activities, but they have to ensure that the whole group (including their subsidiaries) as well as third parties involved in the business relationships (suppliers, buyers, other business relationship) respected human rights and environmental protection standards, both when operating at national level and in other jurisdictions[49]. Therefore, companies globally operating in the countries with the lower standards as compared with the ones at their home country and inter-

[45] See, *e.g.*, F. Möslein, K.E. Sørensen, *Sustainable Corporate Governance, etc.*, cit., p. 4.
[46] See, *e.g.*, BIICL, *Civic Consulting and LSE Consulting Study*, cit., pp. 214-218 and p. 225. For example, in that respect it was also submitted that it should be avoided profiting at the expense of others (see, C. Mayer, *The Governance*, cit., pp. 5-7).
[47] See, BIICL, *Civic Consulting and LSE Consulting Study*, cit., pp. 218-222 and pp. 243-250; G. Ferrarini, *Corporate Purpose*, cit., pp. 41-42.
[48] See, *e.g.*, the *UN Guiding Principles on Business and Human Rights*, cit., pp. 13-21, the *OECD Guidelines for Multinational Enterprises*, cit., and the *OECD Due Diligence Guidance for Responsible Business Conduct*, cit.
[49] *Ibidem.*

nationally recognized as gatekeepers have to ensure through essentially contractual devices and purchasing practices that their subsidiaries and business partners abroad comply with those higher standards.[50] Having this in mind, in a similar vein as it was already mentioned in relation to the corporate purpose, imposing a task upon companies through the mechanism of the corporate duty to carry a mandatory due diligence in a supply chain or value chain raises an issue as to the role of the companies in contemporary society. On the other hand, a due diligence being a context-specific and risk-based is also viewed as a defense to liability of the company[51].

Although dealing with the adverse impacts of corporate activities on society through a mechanism of due diligence is not without its own problems (e.g. challenges to gather information for risk assessment, administrative and financial burden for small and medium sized business, legal uncertainty in relation to a clarification of the scope of the internationally recognized responsible business conduct standards, proportionality as to the scope and content of a due diligence, ability to control and influence business partners, extraterritoriality, applicable law, enforcement, etc.), several jurisdictions aiming to induce companies to better internalize externalities generated by their operations have adopted mandatory corporate due diligence legislation, some are going through the processes of preparation the legislative initiatives[52].

The national regulatory approaches towards corporate due diligence for adverse human rights and environmental impacts resulting from business activities seem, however, to be different both in scope (companies, areas, chain) and the liability model as well as its enforcement.

For example, in 2017, France adopted legislation requiring large French public companies to establish and implement a vigilance plan aimed to identify risks and prevent serious violations of human rights and fundamental freedoms, personal health and safety and the environment that result from their world-wide activities of the group and contractors and suppliers with an established business relationship (*i.e.*, regular, significant and stable) when those activities are linked to this

[50] Also see, P.H. Conac, I. Urbain-Parleani, *The 2017 Act on the duty of vigilance of parent and outsourcing companies*, «Revue trimestrielle de droit financier», 2017.3, pp. 90-96.
[51] See, BIICL, *Civic Consulting and LSE Consulting Study*, cit., p. 20, pp. 110-112, and p. 252.
[52] *Ibidem*, pp. 170-172, pp. 192-213, and pp. 239-242; M. Krajewski, F. Wohltmann, K. Tonstad, *Mandatory Human Rights Due Diligence in Germany and Norway: Stepping, or Striding, in the Same Direction?*, *«Business and Human Rights Journal»*, vol. 6 (2021), pp. 550-558, also available at «SSRN»: https://ssrn.com/abstract=3926360 .

relationship[53]. The actual scope of the legislation is enlarged due to the indirect effect of the law on contractual partners and foreign parents of large French subsidiaries[54]. In France, alongside with the company's obligation to adopt and publicly disclose a vigilance plan in case of its failure to comply with the duty through the judiciary, and a public fine for a false disclosure imposed by securities oversight authorities, a French company may incur civil liability for damages with respect to harm that could have been avoided if the company had fulfilled its statutory requirements to design the plan and implement it[55].

In 2021, Germany has also adopted a mandatory human rights and certain environment-related due diligence requirement for certain large companies, albeit of any legal form, that have their legal or real seat (central administration, principal place of business, administrative headquarters) or a branch in Germany, covering company's own business (including subsidiaries), their direct suppliers as well as indirect suppliers to a limited extent, both in Germany and abroad[56]. While in Germany, the corporate mandatory due diligence model is predominantly premised on public disclosure by reporting about actions German companies have taken in preventing and mitigating adverse impacts on society in their supply chain, as well as public enforcement rules (public fine, exclusion from public procurement) and does not provide for a civil liability through a private enforcement[57].

[53] French companies (registered as either a public limited liability company (*Sociétés anonymes*) or partnership limited by shares (*Sociétés en commandite par actions*)) having their legal seat in France and at group level with at least 5,000 employees in France or 10,000 worldwide for two fiscal years have to establish a vigilance plan: see, P.H. Conac, I. Urbain-Parleani, *The 2017 Act on the duty of vigilance of parent and outsourcing companies*, cit., pp. 90-96.

[54] *Ibidem*, pp. 92-93.

[55] *Ibidem*, pp. 94-96.

[56] If the parent company has a decisive influence over the subsidiary, to comply with the due diligence obligations, the parent company has to include business area and supply chains of the subsidiary as well. See., *e.g.*, M. Krajewski, F. Wohltmann, K. Tonstad, *op. cit.* Since 2023, different types of companies with at least 3,000 employees have a duty. From 2024, the threshold is reduced to 1,000. Foreign companies without a real seat or domestic branch in Germany will not fall under the scope of the law even if they supply goods and services on the German market. Federal Ministry of Labour and Social Affairs, Supply Chain Act, available at: https://www.csr-in-deutschland.de/EN/Business-Human-Rights/Supply-Chain-Act/FAQ/faq.html .

[57] It is, nevertheless, submitted that liability claims on general tort law should not be excluded. See, *e.g.*, M. Krajewski, F. Wohltmann, K. Tonstad, *Mandatory Human Rights Due Diligence in Germany and Norway: Stepping, or Striding, in the Same Direction?*, cit.,

In the context of tackling the phenomena of corporate externalities, an increasing role of the national courts should be emphasized as well[58].

Growing attention as to how better minimize negative impacts of corporate operations in society was not unnoticed at the European level. Alongside with the existing legal instruments related to sector- or issue-specific due diligence and functionally similar measures as well sustainability reporting requirements,[59] a need for the EU intervention establishing a mandatory corporate due diligence requirement at the EU level is currently considered. According to the summary feedback to the public consultation on sustainable corporate governance initiative, built on *BIICL, Civic Consulting and LSE Consulting Study* on the subject-matter and launched by the European Commission, majority of overall respondents supported the need to develop an EU legal framework for due diligence[60].

In March 2021, the European Parliament by its resolution encouraged the European Commission taking a harmonized approach on mandatory corporate due diligence for EU-companies and third country-companies operating within the EU – large companies, publicly listed small and medium-sized companies and small and medium-sized companies operating in high-risk sectors to tackle adverse impacts on human rights, the environment and good governance through their own activities and the value chains[61].

Although, at this stage, it is difficult to debate about forthcoming legislative solutions, in the overall complex and global setting in better tackling negative corporate externalities, the European legislative initiative concerning corporate due diligence on human rights and environmental impacts across supply chains would build a level playing for companies

pp. 7-9.

[58] See, A. Hösli, *Milieudefensie et al v. Shell: A Tipping Point in Climate Change Litigation against Corporations?*, «*Climate Law*», vol. 11.2 (2021) (brill.com) ("The District Court of The Hague's decision in the matter of *Milieudefensie et al. v. Shell*, issued in May 2021, is an unprecedented ruling, holding a fossil-fuel company accountable for its alleged contribution to climate change"). See, also, BIICL, *Civic Consulting and LSE Consulting Study*, cit., pp. 175-177.

[59] See *Recital* Z of the European Parliament, *Resolution with recommendations to the Commission on corporate due diligence and corporate accountability*, of 10 March 2021 (2020/2129(INL)) (2021/C 474/02), P9_TA(2021)0073; see also BIICL, *Civic Consulting and LSE Consulting Study*, cit., pp. 167-169.

[60] European Commission, *Summary report – public consultation on sustainable corporate governance initiative* (26 October 2020 – 8 February 2021), cit., p. 4.

[61] European Parliament, *Resolution with recommendations on corporate due diligence*, cit.

in the internal market. This measure could be useful in better tackling negative international spillovers generated by the EU[62].

4. Concluding remarks

Possible regulatory measures (voluntary soft-law approach and permissive regulations, hard law legislative solutions, targeted either to procedural or substantive rules, smart mix) is an ongoing and heated debate topic on the potential of Company law through corporate governance framework to better deliver to the sustainable development. And in the light of these developments, at the European level, we also witness ambitious goals aimed at contributing towards more sustainable corporate governance framework. Have a moment and see whether a search for the most suitable ways for companies to do more in contributing to sustainable development may cause a revolutionary paradigm-shift in European company law.

[62] *Europe Sustainable Development Report 2021*, cit., pp. viii-xi, pp. 15-21, and pp. 27-28.

The Emerging Law of Sustainable Corporations

Chronicles from a Course, a *Colloquium*, and a *Symposium*

Edited by Maurizio Bianchini and Alan R. Palmiter

PADOVA UP

PADOVA UNIVERSITY PRESS



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First edition 2022, Padova University Press

Original title: The Emerging Law of Sustainable Corporations.
Chronicles from a Course, a *Colloquium*, and a *Symposium*

© 2022 Padova University Press
Università degli Studi di Padova
via 8 Febbraio 2, Padova
www.padovauniversitypress.it

Graphic design Padova University Press

ISBN 978-88-6938-333-5

La pubblicazione di questo libro si è resa possibile grazie al supporto finanziario del Dipartimento di Diritto Privato e Critica del Diritto dell'Università di Padova, nell'ambito del Progetto d'Ateneo per il Miglioramento della Didattica (bando 2019).

The publication of this book was sponsored by the Department of Private Law and Critique of Law of the University of Padova, within the Padova University Project for the Teaching Enhancement (funding call 2019).

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The twenty essays composing this book document a three-fold educational project built around a "Law of Sustainable Corporations" course, organized by the School of Law of the University of Padova, within the Padova University "Miglioramento della Didattica" (Teaching Enhancement) mission, and co-taught by professors Alan Palmiter (Wake Forest University, School of Law) and Maurizio Bianchini (Padova University, School of Law) during the Spring 2021. The LSC course was complemented by a series of *Colloquia* and an end-of-course international *Symposium*, whose proceedings are published in the second and in the first part of the book, respectively, whereas the third part is dedicated to the best eight short essays submitted by Padova students as their LSC course's final written assessment.

Each of three parts this volume consists of represents an endeavour to delineate and to account for some of the most significant issues that are currently shaping the fascinating *journey* into the complex, articulated, multidimensional realm of "corporate sustainability" problems, which are deemed to extend beyond the usual legal survey of the conditions upon which a business organization could qualify as an economically and financially viable concern in a mid to long-term perspective. Upon the premise that the incorporated firm – *i.e.*, the typical for-profit company that, albeit in different fashions, intensively populates and dominates the globalized economy – firmly and strategically stands at the intersection of the 17 Sustainable Development Goals set forth in the UN's 2030 Agenda for Sustainable Development adopted in 2015, the book contributors – academics, experts, and law students – offer the reader a diversified (and sometimes diverging), substantive, cutting-edge analyses on several different aspects of corporate sustainability, including the corporate purpose «jigsaw», the role of institutional investors *vis-à-vis* sustainable and socially responsible investing, the new sustainability provisions impacting corporate reporting and corporate governance structures, the sustainability-oriented principles emerging in the banking sector, the alternative business form represented by the benefit companies, the interactions between principles of corporate crimes and principles of sustainable corporate compliance and risk management, the stakeholders-oriented approach in corporate insolvency, and more.

The *leitmotiv* underpinning the essays collected in the book lays in the multi-prong question about whether, to what extent, and how for-profit companies – and thus their directors, managers, shareholders, and the institutional investors engaging with them and with other stakeholders in various forms – could leave behind their traditional design, as well as the well-established principles currently shaping their usual corporate governance posture, so as to transform themselves, from social costs « externalizing machines», into sustainable business vehicles, operating within the stringent boundaries of legal restrictions, not just in a socially responsible fashion, but, more comprehensively, as *ESG-compliant* market players: that is, within a deeply renovated mindset that could be hopefully characterized by what Alan Palmiter in his concluding essay called a new era of «awakening capitalism».

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ISBN 978-88-6938-333-5

9 788869 383335

€ 20,00