FESE response to Commission consultation on Sustainable Corporate Governance

Brussels 8th February 2021

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

Q1. 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:

FESE welcomes the opportunity to provide a response to the Commission consultation on sustainable corporate governance. We fully support the European Green Deal, the Sustainable Finance agenda and the global transfer of assets to a more sustainable economy to protect the earth and its natural resources for the next generations.

It is important to keep in mind that financial markets reflect developments in other parts of the economy and the sustainable finance agenda cannot, by itself, realise the goals of the Paris Agreement. Real change can be achieved by adopting sector specific regulations and tax incentives to promote the fight against climate change. Ultimately, a shift in all economic agents' mind-set is the most crucial component of a successful transition to a low-carbon and resource-efficient economy that is geared towards inclusive growth and awareness of long-term risks.

In this regard, a comprehensive body of legislation to protect the environment has been adopted and more is to follow in the context of the European Green Deal. Social factors are, for instance, reflected through the European convention on human rights which is part of the EU treaties as well as other international agreements and regulations focusing on human rights, gender equality, labour law, employee engagement, consumer protection, data protection and privacy. Governance factors have been adopted in corporate law in accordance with the European legal tradition, notably on accountancy, transparency and disclosure, shareholder rights, anti-bribery and anti-corruption policies.

The above-mentioned regulations already reflect the interests of stakeholders and are harmonised and enforced within the EU. This approach is highly supported by FESE.

Corporations play a vital role in sustainable development and economic growth. A wide range of interests are important to companies depending on, for instance, the type, size and organisation of the business. We are convinced that all the interests listed above are relevant for the company shareholders and believe companies do take such interests into account. It is ultimately the shareholders who can have a say in the management of a company on how to manage in compliance with applicable legislation.

Since different companies cannot be managed the same way, we support maintaining principles for corporate governance in the existing format of codes. This way, companies are provided with useful guidance on governance, while allowing shareholders to decide on the best ways forward. Many corporate governance codes already include principles regarding, for instance, employee rights, human rights, diversity, and environmental aspects. We believe further developments of such principles should be made within the framework of corporate governance codes.

In addition, the EU could develop a non-binding framework to frame discussions between directors and stakeholders and allow directors to clarify their ESG key performance indicators (KPIs) to relevant stakeholders, following the publication of their relevant ESG disclosure obligations (which will be strengthened in the upcoming NFRD review). This would be helpful without being too prescriptive.

By maintaining principles for corporate governance in the existing format of codes, EU companies would not be exposed to competitive disadvantages compared to companies from outside the EU. However, if any mandatory duties within sustainable corporate governance were to be implemented; small and medium size enterprises (SMEs) and companies with limited resources should be exempted.

As we are transitioning to a more sustainable economy, it is important to recognise companies' best efforts and that companies that are implementing changes to become ESG compliant are not excluded from related initiatives or funding opportunities.

Q2. 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 should be noted that NFRD already requires companies in scope to identify the principal risks related to their business and how these are managed. In line with the Commission's objectives for companies to provide further transparency on their ESG activities, FESE believes that the scope of the NFRD should be harmonised across Member States and

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include an EU level obligation for non-listed companies with more than 500 employees to disclose such non-financial information.

Such requirements should not be introduced to SMEs due to the administrative costs and burdens deriving from such obligations. We believe that there should instead be a voluntary and simplified standard and/or reporting format for SMEs. The NFRD review should introduce a set of voluntary ESG standards dedicated to companies with less than 500 employees. This specific reporting framework should be proportionate to the specific situation of SMEs, to incentivise reporting on their respective ESG activities.

ESG risks vary between individual companies and across industries. Differences may arise with respect to products, processes, organisational structure, business relationships and geographical location. One size does not fit all, and an EU legal framework should therefore be avoided. FESE believes it should be sufficient to ask companies to follow existing guidelines and standards. Many companies are already engaged in processes and risk management related to supply chains and are following principles and guidance developed for this purpose. Such principles should remain 'guidance', i.e. not in a binding legislative framework.

We believe there would be benefits in continuing to build on the OECD guidelines (OECD Due Diligence Guidance for Responsible Business Conduct). Harmonisation at a global level would be especially helpful for companies with international supply chains as would developing sectoral guidance. We would support the development of a common understanding at EU level, building on the work of the OECD, which could take the form of guidelines. Thereafter it would be possible to focus on how to put appropriate processes in place.

Should a legislative proposal be presented, it is important to make a distinction between SMEs and large companies. Establishing a mandatory due diligence policy at EU level would impose additional administrative burdens and costs on SMEs. It is therefore important to exclude SMEs from having to follow due diligence requirements and adapt requirements in line with the (scope of) proposed disclosure obligations under the upcoming NFRD review.

In addition, we emphasise that, if legislative binding-measures were to be adopted, the due diligence liability and duty of care must be binding for all similar companies regardless of whether they are listed or not. Such policies would otherwise disincentivise potential issuers from going public, which would be to the detriment of capital markets and the further development of the EU single market.

Finally, the issue of liability needs to be addressed. We would caution against measures that could potentially lead to a disproportionate liability against third parties.

Q3. 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

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☐ 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

Q3a. 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:

We fully support the European Green Deal, the Sustainable Finance agenda and the global transfer to a sustainable economy. Since companies are different and cannot be managed the same way, we support maintaining principles for corporate governance in the existing format of codes. This way, companies are provided with useful guidance on governance, while allowing shareholders to decide on the best ways forward. Many corporate governance codes already include principles on for instance employee rights, human rights, diversity, and environmental aspects. We believe further developments of such principles should be made within the framework of corporate governance codes.

It is important that any EU due diligence duty is proportional and does not increase administrative costs and procedural burdens, notably for SMEs. As mentioned under Q2, undue legal liability risks can be expected, which is why any potential EU legislative action should set out necessary limitations for legal actions against companies.

Section II Directors' duty of care - stakeholders' interests

Q5 Which of the following interests do you see as relevant for the long- term success and resilience of the company?

	Relevant	Not relevant	I do not know/I do not take position
the interests of shareholders	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 communities 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	X		

the interests of society, please specify:

There is a need to further clarify the definitions that refer to 'the interests of society' to avoid any conflict of interpretation if any guidance should be presented. This equally applies to 'persons and communities affected by the operations of the company'.

Since companies are different and cannot be managed the same way, we support maintaining principles for corporate governance in the existing format of codes. This way, companies are provided with useful guidance on governance, while allowing shareholders to decide on the best ways forward. Many corporate governance codes already include principles on, for instance, employee rights, human rights, diversity, and environmental aspects. We believe further developments of such principles should be made within the framework of corporate governance codes. We would support developing a common understanding at EU level building on the work already carried out by the OECD. This could take the form of guidelines.

other interests, please specify:

Firstly, we disagree with the statement in the question that a director's duty of care is insufficiently defined. This is a long-standing basic principle of company law and in many countries a director's duties are elaborated upon in recommendations in corporate governance codes.

Alongside the interests of shareholders, we believe other financers of a company are relevant, for instance banks who provide loans, or investors in corporate bonds.

We completely agree that various stakeholders' interests contribute to the long-term success, resilience and viability of a company. Companies also take such interests into account since they are an integral part of the financial interests of the company and the

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shareholders. We reiterate that we believe this is why many corporate governance codes include principles on how to take various interests into account.

We see risks with introducing detailed requirements related to certain interests, given that there are a multitude of interests which could inadvertently be excluded. Attempting to encompass and regulate all these interests in detailed ways would in our view be counterproductive. It is therefore preferable to apply principles which can be applied in the best way for each company's specific situation. The interests listed above (and additional ones) are important to many existing or potential shareholders and we encourage further work aiming at ensuring that shareholders can engage and use their rights to the full extent, including by digital solutions.

Q6. 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?

Please rate as follows: 1= I strongly agree, 2= I agree to some extent, 3= I disagree to some extent, 4= I strongly disagree,

	1	2	3	4	I do not know	I do not take position
Identification of the company´s stakeholders and their interests				X		
Management of the risks for the company in relation to stakeholders and their interests, including on the long run				X		
Identification of the opportunities arising from promoting stakeholders' interests				X		

Please explain:

These kinds of considerations are already included in many corporate governance codes, which we believe is the right way forward. Legislative measures moving the above-mentioned duties specifically to directors, would be an inappropriate transfer of responsibility from society to individuals who are not elected by society to carry out such duties.

Since companies are different and cannot be managed the same way, we support maintaining principles for corporate governance in the existing format of codes. This way, companies are provided with useful guidance on governance, while allowing for shareholders to decide on the best ways forward for the company in question. Many corporate governance codes already include principles on, for instance, employee rights, human rights, diversity, and environmental aspects. We believe further developments of such principles should be made within the framework of corporate governance codes.

It should be noted that NFRD already requires companies in scope to identify the principal risks related to their business and how these are managed. In line with the Commission's objectives for companies to provide further transparency on their ESG activities, FESE believes that the scope of the NFRD should be harmonised across Member States and include an EU level obligation for non-listed companies with more than 500 employees to disclose such non-financial information.

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Such requirements should not be introduced to SMEs due to the administrative costs and burdens deriving from such obligations. We believe that there should instead be a voluntary and simplified standard and/or reporting format for SMEs. The NFRD review should introduce a set of voluntary ESG standards dedicated to companies with less than 500 employees. This specific reporting framework should be proportionate to the specific situation of SMEs, to incentivise reporting on their respective ESG activities.

Q7 - 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:

FESE believes that a company's executives, rather than the board of directors, are responsible for the setting up of business procedures (and where relevant; measurable targets). Corporate directors have the role of assessing risks and opportunities, whilst executives ensure that possible risks and adverse impacts are identified, prevented and addressed. We believe it would be counterintuitive to make corporate directors accountable for setting up and enforcing measurable targets within a company.

In principle, we agree with the EU setting a principles-based approach via the use of non-binding guidance for executives to set up adequate procedures, and where relevant, a framework for companies to apply proportional and measurable targets. A limitation to the topics that are essential for stakeholders would be a target-oriented approach, as, for example, identifying, preventing and addressing all possible ESG risks of all stakeholders would result in unjustified effort. The use of the Stakeholder Materiality Analysis tool, which was introduced by the Global Reporting Initiative (GRI) could be an efficient solution to comply with the proposed requirements.

We would highlight the principles already developed by OECD on Due Diligence Guidance for Responsible Business Conduct. Such guidance is helpful and should remain the way forward. We encourage the EU to cooperate with the OECD to facilitate international harmonisation in this regard. Furthermore, we are strongly convinced by the benefits of disclosure. To further the development of disclosures, we believe the Non-financial Reporting Directive is the best tool.

Q8 - 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:

We believe the phrasing of the question is biased in the way that it suggests that balancing the interests of all stakeholders would be the preferred. It does not differentiate but presents two (seemingly opposing) alternative situations to decide upon. However, the situations outlined are too simplistic. There can for instance be situations where short-term decisions need to be taken to preserve the long-term value creation for the sake of stakeholders.

The key role of corporate directors is to focus on the long-term financial interests of the company. We strongly agree that it is a natural part of directors' duties to balance the interests of all stakeholders, as this is relevant for the short- as well as longer term interests of shareholders. It is our experience from operating public markets in several European jurisdictions, that listed companies naturally need to apply long-term horizons. The transparency framework which is a well-developed and natural part of being listed on a stock exchange, inherently contributes to long-termism, or else companies could not attract investors on the public markets.

Guidance on this should remain in recommendations related to corporate governance. As it is already the role of corporate directors to balance the interests of all stakeholders, we strongly disagree that this duty of care needs further clarification in legislation.

Q9 - Which risks do you see, if any, should the directors' duty of care be spelled out in law as described in question 8?

The proposed duty of care would give rise to interpretative uncertainty for directors and related stakeholders. There is also a risk in transferring responsibilities from society to individuals who are not publicly elected. Stakeholders having the impression of being at a disadvantage could file a suit against the company which would increase legal risks. Potential risks also include increase of costs and procedures, bureaucracy and inability in decision-making.

Balancing many interests is a natural part of directors' duties and principles related to this are already included in many corporate governance codes, which we believe is the best solution. However, meeting every stakeholder interest might not always be possible, provable and may lead to a competitive drawback as markets outside EU-law would be less regulated.

If the directors' duty of care were to be spelled out in law, this would lead to directors being exposed to more risks and responsibilities in their role. This would create a new form of accountability which would deter experienced candidates from becoming a

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director of a company, notably if the company faces difficulties in transitioning to more sustainable activities and, consequently, in balancing the interests of all stakeholders. Instead of contributing to the long-term success, resilience and viability of such companies, including directors' duty of care in law would adversely make the companies more vulnerable.

How could these possible risks be mitigated? Please explain.

We believe further developments should be made within principles-based recommendations in corporate governance codes, in the form of soft law instruments. An effective monitoring of the application of these instruments should be implemented. It is essential to prevent and address, within the duty of care, only those risks and impacts which are supported by measurable evidence and could be reasonably justified in relation to the long term interests of the company.

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

A balance of stakeholder interests is already a requirement for sustainable investments, as part of ESG ratings. These requirements are part of an international sustainability policy.

The market share for sustainable financial products is steadily rising as shareholders consider ESG criteria (including the integration of stakeholder interests) to be very important. The integration of stakeholder interests is also discussed in Annual General Meetings.

In this context, we can share various observations regarding its development over the last few years. For instance, it is our clear sense that broader topics such as human rights and environmental aspects are a natural part of company roadshows nowadays.

Furthermore, the sustainable bond market has grown exponentially in recent years. This includes green bonds as well as social bonds, and even blue bonds. Issuances are significantly oversubscribed.

We note significant interest and uptake in the range of products and services developed and offered to various types of stakeholders within the financial ecosystem.

In addition, institutional investors such as pension funds are changing their investment strategies and are including more and more sustainable investments.

These examples demonstrate that investors as well as companies - the whole company and not only directors - are taking an interest in issues such as the environment and human rights into account. Investor interest is already a strong incentive, which has had a huge impact on companies and sustainable corporate governance.

Q10 - 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

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☐ I strongly disagree

☐ I do not know

☐ I do not take position

Please explain:

We strongly disagree with the statement that companies often do not have a strategic orientation on sustainability risks, impacts and opportunities. It is not accompanied by concrete, unbiased evidence, which is unfortunate and does not adhere to the better regulation principles of the European Commission. On the contrary, as elaborated under Q9, we see significant evidence that sustainability is at the core of companies' strategies. It is already integrated in most companies' strategy, decisions and internal oversight.

Recent ECB publications* confirm that ESG risks are seen as drivers of traditional risks. Based on this, the business model and individual exposure to ESG risks should be taken into account when integrating these considerations into the company strategy.

Strategic orientation on sustainability risks, impacts and opportunities should be left at the discretion of companies' directors, notably in their integration within the company (which executives are responsible for). To ensure flexibility, there should be no EU intervention in this respect. Guidance should remain in recommendations related to corporate governance. We strongly disagree that this duty of care needs further clarification in legislation.

*https://www.bankingsupervision.europa.eu/ecb/pub/pdf/ssm.202011finalguideonclimate-relatedandenvironmentalrisks~58213f6564.en.pdf

Q11 - 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:

There are many examples of shareholder initiatives being organised across Europe, including Aviva Investors initiative; Enforcement right of minority rights of shareholders incorporate in German Stock Corporation Act (appointment of a representative of Shareholders to investigate certain transactions of the companies).

In the Nordics and the Baltics as well as in Germany, we observe that company law already includes for instance minority shareholders protection and employee representation. Labour law also comes into play. For instance, the requirement for companies of a certain size to have employee representation on the board is a system with many benefits. In countries where this is not the case, such a system could be explored. These examples, minority shareholder protection and employee board representation, facilitate dialogue and in practice prevent divisive conflicts and "enforcement", which in our view contributes to an outcome where many interests are taken into account, exactly in line with intentions expressed by the Commission in this consultation. When needed however, company law provides certain rights for minority shareholders which are already relevant.

In this context it is also relevant to encourage sharing of best practices as regards employee share schemes. Such schemes have multiple benefits, including engaging employees as shareholders in the company.

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Q12 - 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:

Please see our answer to Q11.

Q13 - 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:

Supervision and enforcement are tasks of the state for good reason. In case of misconduct, competent authorities should investigate and pursue the case. In addition, individuals, whose rights are directly violated by a given company, are entitled to bring action before a competent court. We thus strongly disagree with granting the above-mentioned groups a role in the enforcement of due diligence obligations as it would breach the basic legal principles mentioned above. We would also like to point out that in some countries laws are already in place that give employees a role in the enforcement of director's duty of care. Depending on the size and legal status of the company, employee representatives must be appointed to the supervisory board. Such supervisory boards have a control function and an advisory and support role vis-à-vis the directors. This model has proven successful and enables the company to represent its interests vis-à-vis the management board.

The proposed enforcement would introduce extreme risk for corporate governance procedures and decision making and it would decrease focus on corporate activities followed by negative stock performance.

The main responsibility of protecting the mentioned interests should lie with society. When legitimate interests are violated by a company, society should naturally enforce this. It should not be the role of the individual interest groups to enforce directors' duty of care. Please also see our answer to Q11.

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Section III: Due diligence duty

Q14 - Please explain whether you agree with this definition and provide reasons for your answer.

We generally agree with the definition and wish to underline that establishing processes is the key feature. This should be done through guidelines.

Q15 - 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.

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☐ 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

Q15a - 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?

N/A

Q15b - 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.

FESE believes that the content of the due diligence duty should be flexible and eliminate complexity for issuers. We believe that a 'principles-based' approach should be coupled with a 'sector-specific' approach which would allow companies to apply relevant principles based on their specific activities. Whilst a 'principles-based' approach would allow companies to meet EU level guidance, while respecting local ESG codes and corporate standards, it would be further strengthened if the EU made it more sector-specific and accessible for companies. A sector-specific approach should focus on the riskiest sectors such as the chemical and building industry, plastic production, agriculture, transport etc. The due diligence duty should only cover measurable issues which can be verified and supported by tangible evidence. Focussing on measurable tangible issues would dispose of the uncertainty otherwise imposed on directors.

The EU should focus on cooperating with the OECD in establishing the OECD Guidance on due diligence as EU guidance. The EU should be engaged in the process if/when the OECD guidance is developed and/or amended. This way, one international standard can be maintained which is more helpful than establishing parallel standards, especially for companies operating in a multinational context. Substantial requirements should be aligned on an international basis leading to clarity and comparability which is important for the financial markets.

In our view, there should be guidance and not mandatory requirements. We believe the best way forward is to combine due diligence guidance with a supervision mechanism that would ensure consistency throughout the EU.

A comprehensive impact assessment should be developed before setting forth any possible legislation.

Any potential requirements should be aligned with the Taxonomy Regulation, as well as the ongoing review of the NFRD. The Platform for Sustainable Finance should play a pivotal role in this exercise.

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Q16 - 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[1] 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

We observe that SMEs want to be on board. They should be provided with opportunities to explain their business without being subject to disclosure obligations which add excessive costs and administrative burdens. We believe that OECD's non-binding guidance is a good start, which can be applied by SMEs. If a lighter and more relevant version could be developed for SMEs, this could be helpful. With regards to the scope of application of the guidance, we underline that this should apply to all companies irrespective of the type of funding they have opted for (i.e. to both listed and non-listed companies). The benefits of due diligence duties are not linked exclusively to listed companies, on the contrary, all companies should make efforts. In addition, we would emphasise that companies are of very varying sizes from the largest blue chips to SMEs. On the public markets, the vast majority of listed companies across Europe are in fact SMEs. This is true not only for the smaller growth markets, but also for the main regulated markets. For this reason, due diligence duties should be developed in a way that allows as many companies as possible to comply, even if they may be very different in terms of e.g. size, type of business, business model and organisation.

[1] https://ec.europa.eu/growth/smes/sme-definition_en

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Q17 - 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

Q17a - 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.

Whilst FESE does not support the introduction of any obligations in respect of due diligence, we believe that third country companies should be subject to the same obligations as similar EU companies, when they are operating in the EU. Global application of guidance would support competitiveness and a level playing field among companies with multinational business activities. A mix of thresholds or criteria could be set up, based on activities, turnover generated in the EU, etc.

Q17b - Please also explain what kind of obligations could be imposed on these companies and how they would be enforced.

Third country companies should be subject to the same obligations as similar EU companies.

Q18 - Should the EU due diligence duty be accompanied by other measures to foster more level playing field between EU and third country companies?

☒ Yes

☐ No

☐ I do not know

Please explain:

We reiterate that the OECD work already developed is the best way forward, not only for material aspects of the guidance but also to achieve as much global harmonisation as possible. The EU should engage closely with the OECD as regards due diligence in supply chains.

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Q19 - Enforcement of the due diligence duty

Q19a - 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 an explanation:

In our view, there should be guidance and not mandatory requirements. We believe the best way forward is to combine due diligence guidance with a supervision mechanism that would ensure consistency throughout the EU. This combination allows companies to apply the guidance deemed most appropriate for their company, while at the same time providing transparency for other stakeholders, such as investors, customers, sub-contractors or other partners. This way, stakeholders may take informed decisions on if/how to engage with each company, while taking into account how a company handles supply chain due diligence. Should a mandatory due diligence duty nevertheless be introduced, we consider that this should be supervised by competent national authorities with a mechanism of EU cooperation/coordination to ensure consistency throughout the EU and avoid gold-plating.

Q19b - 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

Section IV: Other elements of sustainable corporate governance

Q20 - Stakeholder engagement

Q20a - 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

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☐ I disagree to some extent

☒ I strongly disagree

☐ I do not know

☐ I do not take position

Please explain:

While we agree that stakeholder involvement and establishing consultation channels for shareholders and employees may contribute to better management of a company, we do not believe the EU should add legal requirements. Where this is not already in place, developing recommendations in soft law, such as corporate governance codes, would possibly be a useful way forward. We observe that many companies already have established active dialogues with a wide range of types of stakeholders depending on the type of business each company operates. Furthermore, we reiterate the points made in Q11 on employee board representation, which may be used as a best practice and implemented in countries where this is not already standard. Minority shareholder rights is also an appropriate and useful principle to build on where this may be lacking. Employee shareholder schemes are also a useful way of engaging employees. There is a wide range of stakeholders which could be relevant in different ways for different companies, depending on the type of business the company operates. Detailing a list of stakeholders seems less helpful and principles-based recommendations should instead be favoured.

Q20c - 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	N/A	N/A
Stakeholder general meeting	X	
Complaint mechanism as part of due diligence		X
Other, please specify	X	

Other, please specify:

- Employee board representation.
- Minority shareholders rights.
- Further measures to facilitate becoming shareholders as well as to exercise shareholder rights, not least by digital solutions.
- Transparency requirements that facilitate for stakeholders to take informed decisions on if/how to engage with a company.
- Many companies are already, depending on the type of business, required to have a complaint function. Whistle-blowing mechanisms can also be useful.

Q21 - Remuneration of directors

	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)	N/A
Regulating the maximum percentage of share-based remuneration in the total remuneration of directors	N/A
Regulating or limiting possible types of variable remuneration of directors (e.g. only shares but not share options)	N/A
Making compulsory the inclusion of sustainability metrics linked, for example, to the company's sustainability targets or performance in the variable remuneration	N/A
Mandatory proportion of variable remuneration linked to non-financial performance criteria	N/A
Requirement to include carbon emission reductions, where applicable, in the lists of sustainability factors affecting directors' variable remuneration	N/A
Taking into account workforce remuneration and related policies when setting director remuneration	N/A
Other option, please specify	N/A
None of these options should be pursued, please explain	7

Please explain:

Intervening in the framework of a company's decision to remunerate its directors based on ESG factors could adversely impact the relationship between the company, its investors and directors.

We favour including recommendations on remuneration of directors in soft law, such as corporate governance codes. Some codes already include for instance a holding period for shares which have been given as remuneration. We believe such principles-based recommendations in combination with transparency provides the best incentives in achieving a balanced remuneration policy. It allows companies to use different benefits and incentive models depending on what may be most appropriate for each company and, for instance, take into account which stage of growth the company is in as well as the competitive situation.

We note that if too many restrictions regarding directors' remuneration are placed on listed companies, there may be an increased reluctance to use the public markets for financing. Further restrictions in this regard would risk conflict with the policy objectives of the Capital Markets Union project, namely, to strengthen European capital markets.

We would take this opportunity to encourage sharing of best practices as regards employee share schemes.

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Q22: Enhancing sustainability expertise in the board

Current level of expertise of boards of directors does not fully support a shift towards sustainability[2], 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 options, please specify

☐ None of these are effective options

Please explain:

Additional rules should not be adopted in this space. It is the board's responsibility to support a shift towards sustainability based on their assessment of the company's business with respect to environmental, social and human rights matters, not through prescriptive rules in relation to its governance. Although we do see merit in board members being exposed to regular ESG training with external science experts and internal experts Specific exceptions should be made for SMEs with limited resources. One size does not fit all and depending on their size and industry, companies should have some room for manoeuvre to enhance sustainability expertise in the board. The question addresses limited competences required for a Board. There are many competences that may be needed on a board - scientific, marketing, communication, engineering, programming, behavioural, environmental, legal, political, artistic, financial, etc., depending on the company's activities. Various research shows that a company with a diverse management performs well. Diversity comes in many ways, including gender, ethnicity, expertise, etc. Applying rules in one particular field would be counterproductive to finding the balance between competence and diversity. Non-binding recommendations in combination with transparency, is the best way forward when it comes to considering a wide range of social and environmental interests.

[2] https://op.europa.eu/en/publication-detail/-/publication/e47928a2-d20b-11ea-adf7-01aa75ed71a1/language-en

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Q23 - 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[3].

(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

Q23a - If you agree, what measure could be taken?

We strongly disagree with the EU taking further action in this area.

(1) Management often opt for dividend payouts and share buy backs because they increase the attractiveness of a share and strengthens the market capitalisation of the company.

(2) This increases the ability of a company to better finance new investments and/or innovation.

(3) Possible regulatory action may create regulatory disincentives to invest in EU domiciled companies and reduce available investment funding that these companies need over the next years to cope with the digital and green transformation and to keep their workforce well-trained and employed. This could impact both retail investors investing into SMEs as well as institutional investors with a global investment universe.

(4) In addition, private savers in Europe who tend to invest their savings in the European Single Market will suffer a disadvantage – either due to lower yields on their investments or higher transaction cost if they would want to invest outside Europe. This is not desirable for the European Union which has individual wealth creation on its political agenda.

[3] https://op.europa.eu/en/publication-detail/-/publication/e47928a2-d20b-11ea-adf7-01aa75ed71a1/language-en

Q24 - Do you consider that any other measure should be taken at EU level to foster more sustainable corporate governance?

If so, please specify

We do not consider that further legislative measures should be undertaken at EU level regarding corporate governance. However, sharing best practices may contribute to sustainable growth, for instance via sustainable corporate governance.

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Section V: Impacts of possible measures

Q25: 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.

	Non-binding guidance.	Introduction of these duties in binding law, cost and benefits linked to setting up/improving external impacts’ identification and mitigation processes	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 0-10	Rating 0 (lowest impact)-10 (highest impact) and quantitative data	Rating 0 (lowest impact)-10 (highest impact) and quantitative data
Administrative costs including costs related to new staff required to deal with new obligations	N/A	N/A	N/A
Litigation costs	N/A	N/A	N/A
Other costs including potential indirect costs linked to higher prices in the supply chain, costs liked to drawbacks as explained in question 3, other than administrative and litigation costs, etc. Please specify.	N/A	N/A	N/A

Better performance stemming from increased employee loyalty, better employee performance, resource efficiency	N/A	N/A	N/A
Competitiveness advantages stemming from new customers, customer loyalty, sustainable technologies or other opportunities	N/A	N/A	N/A
Better risk management and resilience	N/A	N/A	N/A
Innovation and improved productivity	N/A	N/A	N/A
Better environmental and social performance and more reliable reporting attracting investors	N/A	N/A	N/A
Other impact, please specify	N/A	N/A	N/A

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Q26 - 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).

N/A