

Mr. Frans Timmermans, Executive Vice President for the European Green Deal
Mr. Didier Reynders, Commissioner for Justice
European Commission, Rue de la Loi 200, Brussels

Regarding: NGO support for the EU Commission plans on Sustainable Corporate Governance and response to criticism

Dear Executive Vice President Timmermans,
Dear Commissioner Reynders,

Our society is facing an unprecedented series of challenges and systemic crises including climate change, resource depletion, environmental degradation, growing inequalities, unfair and exploitative conditions of workers to cite just some of the most important and urgent.

The EU is striving to transform an unsustainable economic and development model towards a more just, equal and environmentally responsible system through an ambitious roadmap set out in the EU Green Deal.

Companies' role is pivotal in meeting the objectives of the EU Green Deal and designing a sustainable future, as they sit at the junction of consumers, investors, workers, scientists and the global marketplace. However, the incentives, measurement and accountability mechanisms which frame their governance have traditionally been defined with regards to financial performance only.

We strongly welcome and support the Commission's intention to launch a Sustainable Corporate Governance initiative to address these gaps. In particular, we recognise the role you have played in championing this initiative and your commitment to bring forward solutions to ensure that sustainability is considered at all levels of corporate decision-making and that accountability mechanisms are in place to prevent and mitigate severe adverse impacts associated with companies.

The Commission's initiative to clarify the role of directors in overseeing the company's reaction to sustainability risks and adverse impacts to people and planet - and realign incentives in this regard - has recently met with opposition from some business associations and investors, that have expressed concerns that such reforms might undermine both shareholder interests and their own financial performance.

The involvement of directors, i.e. those who lead and steer companies, is paramount to ensuring that companies are able to consider, and take the necessary strategic decisions with regard to the management and oversight of sustainability risks and impacts, both from the perspective of their own success as well as that of their responsibilities to society.

Tackling issues such as climate change or human rights and environmental harm in global value chains often requires profound changes to a company's strategy, financial planning, and more often than not, the business model itself. This requires directors' engagement at levels more senior than corporate sustainability units and decisions and actions that extend far beyond the responsibilities of such units. Moreover, better integration of sustainability matters in businesses' governance will increase the resilience and readiness of companies to face the challenges of today and tomorrow, as well as to seize opportunities stemming from the unprecedented redirection of public and private capital toward climate transformation and sustainability.

Leaders from the business and investor sector have [publicly supported](#) the EU Sustainable Corporate Governance initiative earlier this year, backed by over 90 company law experts and academics. Recent studies also demonstrate both the need for, and feasibility of, such action:

- [Results](#) from the public consultation by the EU Commission on the sustainable corporate governance initiative published this week show overwhelming support (86%) to integrate sustainability risks, impacts and opportunities into company's strategy, decisions and oversight (including 70% of respondents representing individual companies and business associations)
- However, currently, companies' strategies do not adequately reflect sustainability risks identified in companies' annual reports. Results from the [analysis](#) of 1000 EU companies' mandatory sustainability reporting reveal that:
 - Less than 15% of companies are integrating sustainability considerations into core business strategy, board discussions, and performance incentives.
 - Only a third of companies disclose climate targets and even fewer (13%) explain alignment with the Paris Agreement or science based targets or consider climate-related risks in all time horizons relevant for climate transformation (6%).

- Just 3.6% of companies are able to demonstrate effective management of their human rights issues, despite the fact that more than half (55%) identify human rights risks.
- Sustainability and long-term criteria are outweighed in executive remuneration and corporate governance, for instance:
 - In French [CAC40 companies](#), less than 10% of CEO compensation is linked to non-financial or long-term criteria (while 67% was directly connected to short-term financial results) in 2019. Only a minority of companies use separate climate-related criteria, which represent on average around 3.5% of the CEO compensation.
 - In 2018, the UK's two largest listed energy companies spent 14 times (BP) and at least 11 times (Shell) as much on their shareholders as they invested in low carbon activity. The same [study](#) found that the four largest food and drink companies paid shareholders almost £14bn – more than they made in net profit (£12.7bn). To put that into perspective, just one tenth of this shareholder pay-out is enough to raise the wage of 1.9 million agriculture workers around the world to a living wage.
 - In 2020, German automotive company BMW paid more than [€1.6 billion in dividends](#) despite requesting subsidies from the German government and relying on state-backed furlough schemes.
 - More than [half of Europe's bank directors](#) are affiliated with highly carbon dependent companies and organisations, with 61% of directors in 15 boardrooms at risk of being climate-conflicted (more than one third of those directors currently holding roles in polluting companies and organisations).

The price of inaction is too high for our planet, society and companies.

The European Commission's initiative is critically needed to clarify expectations about how directors should engage with sustainability and to ensure meaningful action is taken. This is important not only to ensure the success of the parallel initiatives on due diligence and sustainability reporting, but it is also indispensable on its own merit to enable companies to be truly sustainable.

The reforms explored by the Commission to clarify directors' role in overseeing sustainability and due diligence are based on best practice and are coherent with existing key aspects of company law and corporate governance codes across Europe. While these vary from one Member State to the next, the Commission's proposals broadly fit within the framework of existing directors' duties, thus enabling Member States and companies to integrate proposed legislative reforms in line with their specific company laws and practice.

Therefore, we call on the Commission to introduce an ambitious legislative proposal outlining how directors must support the pillars of corporate transparency, due diligence, and accountability.

We also respectfully urge national governments, large companies and SMEs to engage in a constructive dialogue with policymakers and other stakeholders toward building the best Sustainable Corporate Governance framework possible for the EU, rather than trying to stifle the debate at its inception.

Endnotes:

- Alliance for Corporate Transparency: [2019 research on the sustainability disclosures of 1000 EU companies pursuant to the EU Non-Financial Reporting Directive](#).
- Oxfam study: [Salaires des pdg du cac 40 : la bourse ou le climat ? Comment la rémunération des dirigeants du CAC 40 incite au court-terme au détriment du climat](#)
- Open letter "[Call to Action on Sustainable Corporate Governance](#)"
- Article by Institute for Human Rights and Business, Business and Human Rights Resource Centre, World Benchmarking Alliance "[Responsibility from the top down: Why human rights due diligence must be a mandated concern of corporate boards](#)"

