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Recommended Citation

Wagner, Constance Z., *Evolving Norms of Corporate Social Responsibility: Lessons Learned from the European Union Directive On Non-Financial Reporting*. *Transactions: The Tennessee Journal of Business Law*. Vol. 19, pp. 619-708 (2018).

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EVOLVING NORMS OF CORPORATE SOCIAL RESPONSIBILITY: LESSONS LEARNED FROM THE EUROPEAN UNION DIRECTIVE ON NON-FINANCIAL REPORTING

Constance Z. Wagner*

I. INTRODUCTION

Business fuels economic growth and development in today's world by producing the goods and services that society needs or wants. Viewed in a positive light, business is "a driver of innovation, a creator of wealth, a harbinger of economic freedom."¹ Some view business solely as a vehicle to generate returns on investment. But the expectations of society regarding business are changing. Increasingly, business owners and managers are being called to account for more than profits and losses. Commentators now question the legitimacy of the view that businesses should focus only on financial return to investors.

One could frame the question more pointedly in the following terms: In its relentless pursuit of improving the bottom line, is business doing more harm than good to society? An observer might reach this conclusion after glancing at recent news headlines, which are full of examples of corporate conduct that falls short of societal expectations and reveals ethical failures on the part of business. Such conduct may have negative impacts on consumers, workers, the environment, and the general public.

Some particularly egregious examples come readily to mind. One headline reads "G.M.'s Ignition Switch Death Toll Hits 100," referring to General Motors' failure, prior to 2014, to recall cars containing defective

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¹Yvan Allaire, *What is the Role of Business?*, WORLD ECONOMIC FORUM (Jan. 22, 2014), <https://www.weforum.org/agenda/2014/01/role-business/>.

ignition switches that could cut off a car's engine and electrical system and disable its air bags, even though it had known about the problem for more than a decade.² One of the reasons for the failure was the company's concern with the cost of fixing the problem.³ Another headline reads "Building Collapse in Bangladesh Leaves Scores Dead," referring to the 2013 Rana Plaza factory collapse that killed more than 1,000 workers in the deadliest disaster in the history of the garment industry.⁴ After an investigation, the cause of the collapse was determined to be the use of substandard materials in violation of local building codes, violations that were overlooked because of bribes that had been paid.⁵ This lack of regard for workers' health and safety attracted international attention because the clothing manufactured under these dangerous conditions bore the labels of well-known brands that were sold through retailers in the United States and Europe.⁶ Once again, cost considerations figured prominently in this case since low-cost manufacturing production in countries like Bangladesh is possible due to lack of safeguards for worker well-being.⁷ Yet another headline reads "Oil Spills Into Gulf After Rig Disaster," referring to the 2010 Deepwater Horizon oil rig explosion that resulted in eleven deaths

² Bill Vlasic, *G.M.'s Ignition Switch Death Toll Hits 100*, N.Y. TIMES (May 11, 2015), <http://www.nytimes.com/2015/05/12/business/gms-ignition-switch-death-toll-hits-100.html>.

³ Christopher Jensen, *In General Motors Recalls, Inaction and Trail of Fatal Crashes*, N.Y. TIMES (Mar. 2, 2014), <http://www.nytimes.com/2014/03/03/business/in-general-motors-recalls-inaction-and-trail-of-fatal-crashes.html>.

⁴ Julfikar Ali Manik & Jim Yardley, *Building Collapse in Bangladesh Leaves Scores Dead*, N.Y. TIMES (Apr. 24, 2013), <http://www.nytimes.com/2013/04/25/world/asia/bangladesh-building-collapse.html>.

⁵ *Id.*

⁶ See Clare O'Connor, *These Retailers Involved in Bangladesh Factory Disaster Have Yet to Compensate Victims*, FORBES (Apr. 26, 2014), <http://www.forbes.com/sites/clareoconnor/2014/04/26/these-retailers-involved-in-bangladesh-factory-disaster-have-yet-to-compensate-victims/#25e2111957c5>.

⁷ Rachel Abrams, *Retailers like H&M and Walmart Fall Short of Pledges to Overseas Workers*, N.Y. TIMES (May 31, 2016), <http://www.nytimes.com/2016/05/31/business/international/top-retailers-fall-short-of-commitments-to-overseas-workers.html>.

and led to what has been called the worst environmental disaster in American history, namely a massive oil spill in the Gulf of Mexico that continued for three months before it could be contained, leading to widespread damage to the ecology of the region, including marine life and wildlife.⁸ Subsequent investigations of these events identified a number of causes, including a series of cost-cutting decisions and use of an insufficient safety system by British Petroleum, the Deepwater Horizon's lessee, and its partners.⁹ In all of these cases, and in the many others that also could be cited for the same proposition, business management seems to have made decisions that placed profits ahead of people and the planet.

These cases, and numerous others like them, raise concerns in the public's mind about the lack of social responsibility and accountability of such enterprises and why their consumer safety, labor, environmental, and human rights records are so poor. Due to such concerns, today's business leaders are increasingly under pressure to answer for these and other negative impacts of their enterprises on society.

The notion that corporations are accountable for their social and environmental impacts has begun to crystallize under the heading of corporate social responsibility ("CSR"). Of course, businesses are expected to operate within the bounds of the law. However, CSR is a broader concept that goes beyond the expectation of legal compliance. CSR implies voluntary choices on the part of business to operate in a manner that re-

⁸ Russell Gold, Guy Chazan & Ben Casselman, *Oil Spills into Gulf After Rig Disaster*, WALL ST. J. (Apr. 26, 2010, 12:01 AM), <https://www.wsj.com/articles/SB10001424052748704627704575204590586862162>.

⁹ *Obama Oil Spill Commission's Final Report Blames Disaster on Cost-Cutting by BP and Partners*, THE TELEGRAPH (Jan. 5, 2011, 11:10 PM), <http://www.telegraph.co.uk/finance/newsbysector/energy/oilandgas/8242557/Obama-oil-spill-commissions-final-report-blames-disaster-on-cost-cutting-by-BP-and-partners.html>; Ian Urbina, *BP Officials Took a Riskier Option for Well Casing*, N.Y. TIMES (May 27, 2010), <http://query.nytimes.com/gst/fullpage.html?res=9C00E1D6113BF934A15756C0A9669D8B63&page-wanted=all>.

For a discussion of the BP Oil Disaster and corporate social responsibility, see Miriam A. Cherry & Judd F. Sneirson, *Beyond Profit: Rethinking Corporate Social Responsibility and Greenwashing After the BP Oil Disaster*, 85 TUL. L. REV. 983, 988–999 (2011).

spects people and the planet even if not mandated by government regulators and is now considered part of sustainable business practice. The parameters, content, and means of achieving CSR are murky, but most commentators agree that CSR is a good thing and we need more of it. One hears criticisms of CSR as a desirable goal for managers from time to time, but more and more those voices are being drowned out by the chorus of proponents of integrating CSR into business strategy.

There are many open questions surrounding CSR, but one of the most important ones concerns the optimal strategies for improving business conduct. One avenue for achieving greater CSR that has emerged in recent years is a disclosure-based approach in which companies voluntarily report on non-financial aspects of their operations and in some cases, quantify risks associated with such aspects and explain how such risks might impact financial performance. This type of reporting has been labelled non-financial reporting, CSR reporting, sustainability reporting, and triple bottom line reporting, among other names. Such terms are used interchangeably in this article. While the term “sustainability” is associated in the minds of some with environmental issues only, its meaning in this context is broader, with the term “sustainability reporting” being synonymous with non-financial reporting.

This disclosure-based approach is an alternative to enhanced government regulation of business and is premised on the notion that enhanced transparency about business operations will lead to improved performance, including improvement on key performance indicators relevant to CSR. Consistent with the notion of CSR itself, CSR reporting has traditionally involved a voluntary commitment by enterprises to disclose matters beyond the financial performance information mandated by government regulators. However, in recent years, a number of countries have begun to mandate non-financial reporting in response to concerns about

the low rates of such reporting and the poor quality of non-financial disclosures. Such mandatory reporting requirements vary widely in scope and content and no uniformity exists among such national laws.¹⁰

A problem plaguing non-financial reporting, both voluntary and mandatory, is the lack of a consistent reporting standard that would permit internal benchmarking and comparison across companies. Many large companies have chosen to use one of the non-financial reporting frameworks developed by the Global Reporting Initiative (“GRI”) (such frameworks collectively referred to as “GRI frameworks”), such as the Sustainability Reporting Standards (“GRI Standards”), making the GRI frameworks the apparent gold standard.¹¹ Typically, however, national laws on non-financial reporting, at least in Europe, do not mandate the use of the GRI frameworks or any other reporting standard. The result is wide variation in the amount and type of information disclosed.

This article contributes to the literature on CSR and CSR reporting by examining the significance of a recent European Union (“EU”) directive mandating that certain large enterprises disclose information about their non-financial performance in key areas of concern to advocates of CSR.¹² Pursuant to EU Directive 2014/95/EU (“2014 EU Directive”), countries that are members of the EU (“Member States”) were required to enact laws containing certain minimum requirements for such reporting by December 6, 2016.¹³ This article also touches on the development of mandatory non-financial reporting in two Member States that have been

¹⁰ For a discussion of mandatory CSR reporting requirements in India and China, see Afra Afsharipour & Shruti Rana, *The Emergence of New Corporate Social Responsibility Regimes in China and India*, 14 U.C. DAVIS BUS. L. J. 175 (2014).

¹¹ *Sustainability Reporting Standards*, GLOBAL REPORTING INITIATIVE, <https://www.globalreporting.org>. The Sustainability Reporting Standards replace the earlier reporting standard, the G4 Sustainability Reporting Guidelines (“GRI Guidelines”). The GRI Standards are required for reports published on or after July 1, 2018. The GRI Guidelines remain available before July 1, 2018.

¹² Directive 2014/95/EU, of the European Parliament and of the Council of 22 October 2014 Amending Directive 2013/34/EU As Regards Disclosure of Non-financial and Diversity Information by Certain Large Undertakings and Groups, 2014 O.J. L 330 [hereinafter 2014 EU Directive].

¹³ *Id.* at art. 4 (discussing “Transposition”).

frontrunners in this area, namely France and Denmark, and their implementation of the 2014 EU Directive into their national laws. Such analysis takes place within the larger framework of the global growth of CSR reporting and the significance of these EU developments for the future of such reporting.

The thesis of this paper is as follows. At first glance, the 2014 EU Directive appears to represent a bold move by European governments, since it has been billed as a mandate of non-financial reporting as a matter of national law that will lead to greater information transparency and exert pressure on low-performing businesses to improve. However, a closer look reveals that the picture is more complicated. Instead of consisting exclusively of a government mandate to report non-financial information, the 2014 EU Directive combines elements of both mandatory and voluntary reporting, representing an interesting mix of public and private actor involvement that seems characteristic of evolving reporting trends for non-financial information.

Although such Directive may result in a greater quantity of disclosure, it may not be as successful in achieving the goal of improved transparency as its proponents have suggested. One reason is that the EU Directive may be considered flawed due to weaknesses identified by the author in several of its key provisions. This conclusion is based also on an examination of the experiences of some Member States that adopted mandatory non-financial reporting requirements prior to adoption of the Directive but did not see an improvement in the quality of reporting as a result, although some saw an increase in the quantity of reporting. Extrapolating from those historical cases to the projected impact of the 2014 EU Directive in Member States, it is possible that more reporting, but not necessarily better reporting, will be the result. The element of government regulation embodied in the Directive may not be a sufficient condition to achieve the policy goal of improved CSR reporting. Other conditions needed to achieve that end and yet to be identified may be missing in some Member States.

Nevertheless, the 2014 EU Directive is an important development because of the signals it sends on the importance of non-financial reporting to corporate stakeholders, as well as the lack of effectiveness of prior

voluntary approaches alone in fostering such disclosure. Moreover, the Directive illustrates that the process of achieving greater transparency by businesses on social and environmental issues is difficult, appears to be evolutionary in nature, and will take more time and effort to accomplish in the years ahead.

As such, the EU experience in this area may provide useful instruction for other countries seeking to achieve similar goals of higher levels of improved non-financial reporting. Lessons from the EU experience may be of particular interest to observers in the United States where the state of CSR reporting is less well-developed compared to that in other countries.

The analysis will proceed as follows. Section II will explore the meaning of CSR and the rationale for use of non-financial reporting as a means to move business in the direction of greater social responsibility. It will also discuss current global developments in non-financial disclosure, including the movement from voluntary to mandatory CSR reporting in some countries. Section III will analyze the growth of non-financial reporting in the EU by tracing the historic development of, and the policy rationale behind, the 2014 EU Directive. It will also illustrate the challenges associated with implementation of non-financial reporting requirements at the national level by referring to the experiences of two Member States that have been leaders in mandating CSR reporting, namely France and Denmark. Section IV will critique the 2014 EU Directive and the trend it represents for non-financial reporting. Section V will conclude.

II. THE MEANING OF CORPORATE SOCIAL RESPONSIBILITY AND THE ROLE OF NON-FINANCIAL REPORTING

This Section II lays the groundwork for an analysis and critique of the 2014 EU Directive. It does so by examining current issues surrounding the meaning of CSR and the role of non-financial reporting in promoting enhanced social responsibility by businesses.

A wide variety of actors have argued that businesses have obligations to conduct their operations in a socially responsible manner. These include those directly involved with businesses such as investors, employ-

ees, and consumers, as well as governments, non-governmental organizations, intergovernmental organizations, and scholars in the fields of management and law. This notion forms the foundation of current discourse on CSR, which seeks to hold businesses accountable for the impacts of their operations.

CSR stands in contrast to the traditional view of the purpose of business, which is to maximize financial return for investors. Economist Milton Friedman advocated for this view in his often-cited 1970 New York Times opinion piece entitled “The Social Responsibility of Business is to Increase Its Profits,” when he stated:

[A] corporate executive is an employee of the owners of the business. He has direct responsibility to his employers. That responsibility is to conduct the business in accordance with their desires, which generally will be to make as much money as possible while conforming to the basic rules of the society, both those embodied in law and those embodied in ethical custom.¹⁴

The view that business managers’ sole responsibility is shareholder value maximization is sometimes referred to as the shareholder primacy theory. This view has been criticized by many others, including law professor Lynn Stout, who argued in her 2012 book entitled *The Shareholder Value Myth: How Putting Shareholders First Harms Investors, Corporations, and the Public* that the shareholder primacy theory is harmful to a wide variety of corporate constituencies, is based on factually mistaken claims about law, and that support for this theory is crumbling.¹⁵

¹⁴ Milton Friedman, *The Social Responsibility of Business is to Increase Its Profits*, N.Y. TIMES (Sept. 13, 1970), <http://www.nytimes.com/1970/09/13/archives/a-friedman-doctrine-the-social-responsibility-of-business-is-to.html>.

¹⁵ Lynn Stout, *The Shareholder Value Myth*, CORNELL L. FACULTY PUBLICATIONS (Apr. 19, 2013), <http://scholarship.law.cornell.edu/facpub/771> (discussing LYNN STOUT, THE

Lynn Stout's view is echoed by numerous commentators. It is safe to say that the shareholder primacy theory is losing its grip and the goal of promoting CSR is gaining ascendancy. As business professor Min-Dong Paul Lee has noted, "[CSR] has been transformed from an irrelevant . . . idea to one of the most orthodox and widely accepted concepts in the business world . . ." ¹⁶ Many businesses are of the view that adopting CSR strategies is not only desirable but necessary. In his 2003 book entitled *The Planetary Bargain: Corporate Social Responsibility Matters*, business professor Michael Hopkins argued that, "[i]n time, it will not be possible to conduct business without being socially responsible . . . [N]ew rules or corporate laws may well be unnecessary, because corporations will see for themselves – and many have seen this already – the need to behave more responsibly in the social arena." ¹⁷

One commentator from the world of social investing has noted that the growth of CSR has been especially noteworthy in Europe. Steven D. Lydenberg, who is affiliated with Domini Social Investments, and who wrote a 2003 book about management strategies to integrate CSR entitled *Corporations and the Public Interest: Guiding the Invisible Hand*, has referred to CSR as "a major secular development, driven by a long-term reevaluation of the role of corporations in society." ¹⁸ In his view, compared to the United States, this reevaluation is stronger in Europe, where the view that companies have duties to stakeholders as well as shareholders has taken hold, noting also that "the European influence will be very hard to resist over the long run." ¹⁹

SHAREHOLDER VALUE MYTH: HOW PUTTING SHAREHOLDERS FIRST HARMS INVESTORS, CORPORATIONS, AND THE PUBLIC (Berrett-Koehler Pub. 2012)).

¹⁶ Min-Dong Paul Lee, *A Review of the Theories of Corporate Social Responsibility: Its Evolutionary Path and the Road Ahead*, 10 INT'L J. OF MGMT. REV. 53, 53 (2007).

¹⁷ MICHAEL HOPKINS, *THE PLANETARY BARGAIN: CORPORATE SOCIAL RESPONSIBILITY MATTERS* xii (Rutledge 2003).

¹⁸ Edward Teach, *Two Views of Virtue*, CFO, (Dec. 15, 2005), <http://ww2.cfo.com/risk-compliance/2005/12/two-views-of-virtue/> (citing STEVEN D. LYDENBERG, *CORPORATIONS AND THE PUBLIC INTEREST: GUIDING THE INVISIBLE HAND*, 31 (Berrett-Koehler Pub. 2005)).

¹⁹ *Id.*

While the notion of CSR has gained traction in recent years, there are numerous conceptual difficulties that have not been settled. The management literature is rich with journal articles and books that have tackled this topic, including the definition of CSR, the rationale for pursuit of CSR by business managers, and the appropriate strategies for promoting greater CSR in business. To a lesser extent, legal scholars have also engaged on this subject, focusing on the fiduciary duties of managers and whether they may lawfully take into account the interests of stakeholders other than shareholders, the use of voluntary codes of conduct seeking to enhance CSR, the promulgation of laws that have codified CSR norms, and the extent and specific content of CSR obligations. While much ink has been spilled, CSR is still an ambiguous concept in several respects.

One often-repeated criticism of CSR is that the definition of this concept is too vague and there is no consensus surrounding the meaning of the term. In fact, a review of the literature discussed herein reveals that there are certain common elements that CSR definitions share. This author believes that the problem lies not with the definition, but with lack of clarity regarding the business rationale for and business strategies needed to achieve CSR, as well as lack of clear guidelines on the content of CSR obligations.²⁰

While the language of CSR definitions may vary, there is some consensus around core concepts. Management professor David Vogel, who wrote the influential book *The Market for Virtue: The Potential and Limits of Corporate Social Responsibility*, defined CSR as “practices that improve the workplace and benefit society in ways that go above and beyond what companies are legally required to do.”²¹ Other definitions are more expansive and generally include the following elements: a voluntary undertaking to engage in conduct that goes beyond what is legally required, a commitment to addressing the interests of a broad spectrum of corporate

²⁰ Daniel Kindermann, *Corporate Social Responsibility in the EU, 1993–2013: Institutional Ambiguity, Economic Crises, Business Legitimacy and Bureaucratic Politics*, 51 J. COMMON MARKET STUD. 702 (2013) (discussing ambiguity of definition and rationale for CSR in Europe).

²¹ DAVID VOGEL, *THE MARKET FOR VIRTUE: THE POTENTIAL AND LIMITS OF CORPORATE SOCIAL RESPONSIBILITY 2* (Brookings 2006).

constituencies or stakeholders other than shareholders, and a focus not only on financial performance, but also on social and environmental performance.

This description of the core concepts found in CSR definitions is consistent with the results of a study on this topic conducted by management professor Alexander Dahlsrud. Dahlsrud analyzed 37 different definitions of CSR and found that, while there was variation in the exact language used, this group of definitions consistently referred to five dimensions: the natural environment, the relationship between business and society, socio-economic or financial aspects including business operations, interaction with stakeholders, and voluntariness that encompassed actions not required by law.²² He concluded that such consistency across definitions made “the lack of one universally accepted definition less problematic.”²³ However, Dahlsrud criticized the definitions for failing to address what optimal CSR consisted of and how to develop strategies to achieve that goal, noting that a successful approach is content specific and the details of specific CSR issues to be addressed and how to engage with stakeholders must be developed for individual businesses.²⁴

An influential definition of CSR was developed by management professor Archie B. Carroll, who has written extensively about many different aspects of CSR. Carroll developed a framework for understanding CSR that identifies four categories of obligations of business to society, namely the economic, legal, ethical, and discretionary.²⁵ In the economic category, Carroll placed the responsibility of business to produce goods and services that society wants and to sell them at a profit.²⁶ Under legal, he placed the obligation for business to fulfill its economic missions within

²² Alexander Dahlsrud, *How Corporate Social Responsibility is Defined: An Analysis of 37 Definitions*, 15 CORP. SOC. RESP. ENVTL. MGMT. 4–5 (2008).

²³ *Id.* at 6.

²⁴ *Id.*

²⁵ Archie B. Carroll, *A Three-Dimensional Conceptual Model of Corporate Performance*, 4 ACAD. OF MANAGEMENT REV. 497, 499 (1979).

²⁶ *Id.* at 500.

the framework of legal and regulatory requirements.²⁷ He defined ethical obligations as societal expectations of business conduct that exceed legal requirements.²⁸ Finally, he described discretionary responsibilities as those involving individual choices to address social issues, which are purely voluntary in nature and not expected in a moral or ethical sense, such as philanthropy.²⁹ In Carroll's view, all four of these responsibilities should be fulfilled by business at all times, meaning that a firm committed to CSR "should strive to make a profit, obey the law, be ethical, and be a good corporate citizen."³⁰

Carroll's definition of CSR is useful in that it brings together the traditional and new responsibilities of business, which he also terms the old and new social contracts between business and society. His definition makes more explicit the notion of CSR when he contends that "the economic and legal responsibilities are 'required', the ethical responsibilities are 'expected', and the discretionary responsibilities are 'desired.'"³¹ It is the scope of these latter two categories, namely the nature and extent of the ethical and discretionary responsibilities that go beyond the economic and legal obligations, that remains subject to debate.³²

Looking at all four categories of business responsibilities in Carroll's definition is also helpful in discussing the rationale for CSR, including the so-called "business case" for CSR, because it includes financial performance in a constellation of obligations that also encompasses the ethical and discretionary activities that many would identify with CSR.

²⁷ *Id.*

²⁸ *Id.*

²⁹ *Id.* In his later writings, Carol would come to collapse these four categories into three, combining the ethical and discretionary, and arguing that philanthropy fell within both the ethical and discretionary domains. See Mark S. Schwartz & Archie B. Carroll, *Corporate Social Responsibility: A Three-Domain Approach*, 13 *BUS. ETHICS Q.* 503 (2003).

³⁰ Archie B. Carroll, *The Pyramid of Corporate Social Responsibility: Toward the Moral Management of Organizational Stakeholders*, *BUS. HORIZONS*, July–Aug. 1991, at 39, 40, 43.

³¹ Archie B. Carroll & Kareem M. Shabana, *The Business Case for Corporate Social Responsibility: A Review of Concepts, Research and Practice*, 12 *INT'L J. OF MGMT. REV.* 85, 90 (2010).

³² *Id.*

The “business case” for CSR refers to a connection between CSR policies and improved corporate performance. There is a large body of management literature that seeks to establish such a link, thereby justifying CSR by claiming that there is a “market for virtue” and that businesses will be “doing well by doing good.”³³

A number of commentators in the field of management studies have traced the development of CSR from the 1950s to the present and noted a shift over time from a focus on being a good corporate citizen by doing good works for society to a focus on benefits to business from CSR policies, namely the “business case” for CSR, with such shift starting in the 1980s.³⁴ Management gurus including Peter Drucker and Michael Porter weighed in on the topic. Peter Drucker proposed a “new meaning” of CSR, contending that profitability and responsibility were not only compatible, but that businesses should view social problems as opportunities that they could be paid to solve.³⁵ As Drucker expressed it, the proper social responsibility of business is “to tame the dragon, that is to turn a social problem into economic opportunity and economic benefit, into productive capacity, into human competence, into well-paid jobs, and into wealth.”³⁶ Michael Porter suggested that companies should connect their philanthropic expenditures “to areas that improve their long-term competitive potential,” which has led some companies to adopt strategic philanthropy by linking their charitable giving to their business missions.³⁷

³³ David Vogel, *Is There a Market for Virtue? The Business Case for Corporate Social Responsibility*, 47 CAL. MGMT. REV. 19 (2005). For an expanded discussion of this topic, see VOGEL, THE MARKET FOR VIRTUE, *supra* note 21.

³⁴ Carroll & Shabana, *supra* note 31, at 87–88; see also Archie B. Carroll, *Corporate Social Responsibility: Evolution of a Definitional Construct*, 38 BUS. AND SOC'Y 268 (1999); Lee, *supra* note 16.

³⁵ Peter Drucker, *The New Meaning of Corporate Social Responsibility*, 26 CAL. MGMT. REV. 53, 55 (1984).

³⁶ *Id.* at 62.

³⁷ Michael Porter & Mark Kramer, *The Competitive Advantage of Corporate Philanthropy*, 67 HARV. BUS. REV. 56, 67 (2002).

Eventually, over time, several different business rationales emerged in the management literature to supplant the earlier social rationales for pursuing CSR strategies, namely reducing cost and risk, strengthening legitimacy and reputation, and gaining a competitive advantage, among others.³⁸ A growing number of academic commentators, along with managers and investors, began to embrace the notion that strategic adoption of CSR could lead to financial rewards in the long run. The so-called “business case” for CSR was premised on the notion that financial performance and social performance were directly linked and was understood to mean that higher profits would result from CSR strategies.³⁹

However, despite repeated efforts by researchers to empirically verify that CSR policies positively affect the bottom line performance of a corporation, the “business case” for CSR has never been proven.⁴⁰ David Vogel noted that evidence of the “business case” for CSR is inconclusive, with some empirical studies showing a positive relationship, some finding a negative relationship, and yet others finding the relationship to be either neutral or mixed.⁴¹ Nevertheless, he stated that “[i]t is not necessary to find a positive statistical relationship between CSR and profits to claim that some firms may benefit financially from being more responsible or suffer from being irresponsible.”⁴² In other words, it has been possible for businesses to justify pursuing CSR strategies based on other perceived benefits apart from a direct link to increased profits.⁴³ A number of commentators have identified other reasons for companies to pursue CSR, often focusing on the importance of engaging with a wide variety of corporate constituencies or stakeholders, including employees, consumers, and

³⁸ Elizabeth C. Kurucz et al., *The Business Case for Corporate Social Responsibility*, in ANDREW CRANE, ET AL., *THE OXFORD HANDBOOK OF CORPORATE SOCIAL RESPONSIBILITY* 83, 86 (Oxford 2008).

³⁹ Vogel, *supra* note 33.

⁴⁰ *Id.*

⁴¹ *Id.* at 29.

⁴² *Id.* at 33.

⁴³ *Id.* at 33–34. (noting that such benefits may be “elusive”).

members of the general public.⁴⁴ Among the non-“business case” benefits that have been suggested are building community ties and maintaining a “social license” to operate, increasing morale and attachment of employees, attracting potential employees, developing future customers, and creating an environment in which the business can prosper.⁴⁵ However, such benefits may prove elusive and will only be obtained for some businesses under certain circumstances.⁴⁶

Although the “business case” for CSR has never been proved, and although other possible benefits to business are hard to pinpoint, many corporations now behave as though it is in their self-interest to pursue CSR policies. An increasing number seek to talk the talk of CSR, although it is not at all clear that they also walk the walk. More and more frequently, businesses are disclosing information about their CSR policies, often on their websites, in various written reports that they issue, and in their advertising.

Currently, there is no agreement on a common set of business activities that constitute socially responsible behavior that everyone agrees on and there is no standardization of disclosure by business of their CSR policies. While there is some consensus around a rather broad definition of CSR, as discussed above, such definition does not clarify the exact content of CSR obligations. This lack of a common understanding of the content of CSR allows businesses to choose the manner in which they portray their business operations in the public arena. While businesses may like such flexibility, this lack of standards is troubling. The danger of failing to specify the components of virtuous corporate behavior is that businesses are then left free to decide what counts as responsible conduct, often to promote their own self-interest and to the detriment of the interests of business stakeholders. For example, in the oil and gas industry,

⁴⁴ Joshua D. Margolis & James P. Walsh, *Misery Loves Companies: Rethinking Social Initiatives by Business*, 280 ADMIN. SCI. Q. 268 (2003).

⁴⁵ Charles J. Fombrun et al., *Opportunity Platforms and Safety Nets: Corporate Citizenship and Reputational Risk*, 105 BUS. SOC’Y REV. 85, 86 (2000).

⁴⁶ Vogel, *supra* note 33.

companies have been accused of engaging in “greenwashing,” the practice of using public relations channels and advertising to promote a “green” image of environmental responsibility while in fact engaging in potentially damaging activities in their business operations.⁴⁷

Various parties, including intergovernmental organizations, non-governmental organizations, business investors, industry groups, and businesses themselves, have sought to fill this void by specifying the content of CSR through a variety of codes of conduct. Such codes can apply to individual businesses, or to businesses in a particular industry or particular region, or they may be global in scope, applying to multinational corporations and a wide variety of other businesses around the world. Generally speaking, these codes of conduct are non-binding and constitute voluntary undertakings that businesses subscribe to, mirroring the definition of CSR itself, which implies conduct that is voluntary in nature. This proliferation of standards is helpful in that there is now some content to CSR for which businesses should be held accountable, although there is no consensus on the exact standards to which businesses should be held and the content of such codes varies widely.

The most influential sets of standards are those that have been promulgated at the international level, including the United Nations Global Compact (“U.N. Global Compact”), the Organization of Economic Co-operation and Development (OECD) Guidelines for Multinational Enterprises, and the Guiding Principles on Business and Human Rights implementing the United Nations “Protect, Respect and Remedy” Framework.⁴⁸ The most widely-accepted of these international initiatives is the U.N. Global Compact, an initiative launched by then United Nations

⁴⁷ For a discussion of greenwashing in the context of the 2010 BP oil spill in the Gulf of Mexico, see Cherry & Sneirson, *supra* note 9, at 985.

⁴⁸ See generally *Who We Are, The Power of Principles*, UNITED NATIONS GLOBAL COMPACT, <https://www.unglobalcompact.org/what-is-gc/mission/principles> (last visited Mar. 18, 2018); OECD (2011), *OECD Guidelines for Multinational Enterprises*, OECD Publishing, <http://dx.doi.org/10.1787/9789264115415-en>; Guiding Principles on Business and Human Rights, UNITED NATIONS HUMAN RIGHTS OFFICE OF THE HIGH COMMISSIONER (2011), http://www.ohchr.org/Documents/Publications/GuidingPrinciplesBusinessHR_EN.pdf.

Secretary-General Kofi Annan, at the World Economic Forum in 1999.⁴⁹ With over 9,000 businesses as signatories in 161 countries, the U.N. Global Compact describes itself as “the world’s largest corporate sustainability initiative.”⁵⁰

The U.N. Global Compact seeks to align business operations and strategies with ten universally-accepted principles in the areas of human rights, labor standards, the environment, and anti-corruption, and to encourage businesses to take actions to advance societal goals.⁵¹ The ten core principles are drawn from United Nations Conventions and Declarations, including the Universal Declaration of Human Rights, the International Labour Organization’s Declaration on Fundamental Principles and Rights at Work, the Rio Declaration on Environment and Development, and the United Nations Convention Against Corruption.⁵²

The U.N. Global Compact invites businesses to subscribe to these principles by becoming members. Members are required to have the approval of their chief executive to participate and are asked to make an annual contribution to support the work of the U.N. Global Compact.⁵³ Members are encouraged to make the U.N. Global Compact and its principles an integral part of business strategy, day to-day operations, and organizational culture; and incorporate the UN Global Compact and its principles in the decision-making processes of the highest-level governance

⁴⁹ Press Release, United Nations Secretary General, Secretary-General Proposes Global Compact on Human Rights, Labour, Environment, In Address To World Economic Forum, U.N. Press Release SG/SM/6881 (Feb. 1, 1999), <http://www.un.org/press/en/1999/19990201.sgsm6881.html>.

⁵⁰ *Our Participants*, UNITED NATIONAL GLOBAL COMPACT, <https://www.unglobalcompact.org/what-is-gc/participants> (last visited Mar. 18, 2018).

⁵¹ *Who We Are, The World’s Largest Corporate Sustainability Initiative*, UNITED NATIONAL GLOBAL COMPACT, <https://www.unglobalcompact.org/what-is-gc> (last visited Mar. 18, 2018).

⁵² UNITED NATIONAL GLOBAL COMPACT, *supra* note 48.

⁵³ *Who We Are, About the Global Compact, Frequently Asked Questions*, UNITED NATIONAL GLOBAL COMPACT, <https://www.unglobalcompact.org/about/faq> (last visited Mar. 18, 2018).

body.⁵⁴ In addition, members are expected to publicly advocate for the U.N. Global Compact through public statements in the form of press releases and speeches.⁵⁵ Finally, members must report to their stakeholders annually through a “Communication on Progress,” that documents progress toward implementing the ten core principles and “[e]fforts to support societal priorities” and can be incorporated in the annual report or a standalone sustainability report.⁵⁶

There are numerous other CSR initiatives that have been developed.⁵⁷ They differ in their source, coverage, scope of responsibilities, and the extent to which they impose affirmative obligations of compliance, monitoring, and third party auditing or assurances.⁵⁸ In spite of such variations, it should be noted that such CSR initiatives frequently focus on four key areas of responsibility, namely respect for the environment, social and labor practices that uphold the rights of workers, respect for human rights, and a prohibition on bribery and corruption in business dealings, although some frameworks cover more and others cover fewer areas.

Apart from the U.N. Global Compact, most other CSR initiatives have had only limited success in attracting businesses that will subscribe to the standards. The most popular standards are those that are deemed most “flexible” by businesses, implying that the standards are malleable. In addition, there usually is little, if any, monitoring of compliance required under any such set of standards. As a result, the success of such standard-setting exercises as a driver for greater corporate accountability is questionable.

⁵⁴ *Id.*

⁵⁵ *Id.*

⁵⁶ *Id.*

⁵⁷ For a listing of other international initiatives, see WIM BARTELS ET AL., CARROTS & STICKS: GLOBAL TRENDS IN SUSTAINABILITY REPORTING REGULATION AND POLICY, KPMG (2016), <https://assets.kpmg.com/content/dam/kpmg/pdf/2016/05/carrots-and-sticks-may-2016.pdf>.

⁵⁸ *Id.*

In addition to voluntary codes of conduct, other approaches to CSR are emerging. In some cases, mandatory legal rules are being put in place rather than relying on voluntary action by business. One example is the U.S. Foreign Corrupt Practices Act, which prohibits bribery in international business transactions, and similar laws in other countries prohibiting such conduct.⁵⁹ An alternative approach to such substantive regulation of corporate behavior is a disclosure-based approach in which businesses issue non-financial reports covering their CSR activities. An increasing number of companies are publishing such reports in addition to the mandated financial reporting required by government regulators. In general, businesses prefer non-financial reporting over government regulation, which may explain the upswing in such reporting in recent years.

Non-financial reporting is sometimes referred to as triple bottom line reporting. John Elkington, founder of SustainAbility, a consulting firm for sustainable businesses, and a leader in the CSR movement, coined this phrase to describe his business accounting framework encompassing three different bottom lines: (1) the traditional measure of corporate profit, namely the bottom line of the profit and loss account, (2) the people account, which measures the social responsibility of an organization's operations, and (3) the planet account, which measures the environmental responsibility of an organization.⁶⁰ In Elkington's view, only businesses that fully account for all three bottom lines—profit, people and planet—are fully accounting for the costs of doing business.⁶¹

⁵⁹ Foreign Corrupt Practices Act of 1977 (FCPA), 15 U.S.C. § 78dd-1, et seq. (2012); There are also international treaties prohibiting bribery in international business, such as the United Nations Convention Against Corruption and the OECD Antibribery Convention. See U.N. Office on Drugs and Crime, *U.N. Convention Against Corruption*, G.A. Res. 58/4 (Oct. 31, 2003); OECD, *Convention on Combating Bribery of Foreign Public Officials in International Business Transactions* (Nov. 21, 1997).

⁶⁰ *Triple Bottom Line*, THE ECONOMIST (Nov. 17, 2009), <http://www.economist.com/node/14301663>. For a further discussion of triple bottom line reporting, see JOHN ELKINGTON, *CANNIBALS WITH FORKS: THE TRIPLE BOTTOM LINE OF 21ST CENTURY BUSINESS* (Capstone 1997).

⁶¹ *Id.*

The rationales advanced for non-financial reporting by corporations mirror those heard for pursuing CSR strategies more generally. Carroll and Shabana have noted that corporations believe they enhance their legitimacy and reputation through disclosure of information about their social and environmental performance by demonstrating that their operations are consistent with social norms and legitimate expectations.⁶² The GRI, an organization promoting sustainability initiatives for business including non-financial reporting,⁶³ believes that companies should provide non-financial disclosure based on “business case” grounds “because being accountable reduces risk and capital costs, attracts and retains customers and staff, supports stakeholder engagement and creates new business opportunities.”⁶⁴ Law professor Virginia Harper Ho focuses on the link between environmental, social, and governance (“ESG”) performance and investment risk and return, noting that financial analysts and investment advisors now use tools to assist investors in determining how firms incorporate ESG information into business strategy, risk management, corporate governance, and value creation.⁶⁵

An increasing number of companies are publishing CSR reports in addition to the mandated financial reporting required by government regulators. The global accounting firm KPMG has examined global trends for non-financial reports among Global Fortune 250 companies, namely the world’s 250 largest companies, noting an upswing in such disclosure

⁶² Carroll & Shabana, *supra* note 31, at 99.

⁶³ “GRI is an international independent organization that helps businesses, governments and other organizations understand and communicate the impact of business on critical sustainability issues such as climate change, human rights, corruption and many others.” *About GRI*, GLOBAL REPORTING INITIATIVE, (last visited Sept. 25, 2017), <https://www.globalreporting.org/Information/about-gri/Pages/default.aspx>.

⁶⁴ FOSTER ELECTRIC REPORT, CERES, OTHERS CALL FOR USE OF NEW ENVIRONMENTAL REPORTING GUIDELINES (2006).

⁶⁵ Virginia Harper Ho, “*Comply or Explain*” and the Future of Nonfinancial Reporting, 21 LEWIS & CLARK L. REV. 317, 322 (2017).

among this group of companies over time.⁶⁶ In its 2015 publication entitled *Currents of Change: The KPMG Survey of Corporate Responsibility Reporting 2015* (“2015 KPMG Report”), KPMG noted that 92% of Global Fortune 250 companies engage in some form of sustainability reporting.⁶⁷ The 2015 KPMG Report also surveyed the N100, namely the 100 largest companies in each of 45 countries, and noted that almost three-quarters of N100 companies reported on CSR.⁶⁸ There are regional differences in reporting practices among companies, with Europe traditionally the leader, although in recent years the Asia Pacific region and the Americas have gained ground.⁶⁹ The 2015 KPMG Report also identified several significant trends in CSR reporting by this group of companies.

KPMG, in conjunction with several other organizations including the GRI and the United Nations Environment Program, has also conducted studies tracing the evolution of such reporting and the characteristics of the instruments that drive reporting. In its 2016 publication entitled *Carrots & Sticks: Global Trends in Sustainability Reporting Regulation and Policy* (“2016 Carrots & Sticks Report”), KPMG and its co-authors noted rapid and significant growth in the total number of instruments that require or encourage organizations to report information about their sustainability performance.⁷⁰ The 2016 Carrots & Sticks Report also highlighted important trends in such reporting that are consistent with those identified in the 2015 KPMG Report.

The first noteworthy trend set forth in these KPMG Reports is the emergence of mandated CSR reporting. Traditionally, companies have

⁶⁶ ADRIAN KING & WIM BARTELS, CURRENTS OF CHANGE: THE KPMG SURVEY OF CORPORATE RESPONSIBILITY REPORTING 2015, at 30 (2015), <https://assets.kpmg.com/content/dam/kpmg/pdf/2016/02/kpmg-international-survey-of-corporate-responsibility-reporting-2015.pdf>. Such reporting fluctuated between 90-95% over the preceding four years.

⁶⁷ *Id.*

⁶⁸ *Id.*

⁶⁹ *Id.* at 31–32.

⁷⁰ BARTELS ET AL., *supra* note 57, at 10.

engaged in CSR reporting on a voluntary basis and many argued that it should remain that way.⁷¹ But that is changing and the most important driver of the recent growth in non-financial reporting is mandatory standards imposed through government regulation and stock exchange rules.⁷² This regulatory growth is especially noteworthy in Europe, the Asia Pacific region, and in Latin America.⁷³ One of the most significant developments is the growth of mandated non-financial reporting in Europe as a result of the historical evolution of EU legal instruments culminating in the 2014 EU Directive, which is the focus of this article.

A second trend relates to where such information is disclosed and whether the information provided is independently verified through third party assurances or auditing. In the past, many companies disclosed such information in standalone reports focusing exclusively on sustainability topics and companies considered third party auditing to be undesirable and therefore optional.⁷⁴ However, according to the 2015 KPMG Report, the trend has shifted and it has become standard practice for the world's largest companies to include CSR information in their annual reports and most of these companies now have their data independently audited.⁷⁵ There is an emerging trend toward "integrated reporting" in which a company issues a single report combining financial and non-financial disclosure and draws the main connections between social, environmental, and economic actions and material outcomes for the company. However, the

⁷¹ KPMG INT'L AND THE UNITED NATIONS ENV'T PROGRAM, CARROTS & STICKS FOR STARTERS: CURRENT TRENDS AND APPROACHES IN VOLUNTARY AND MANDATORY STANDARDS FOR SUSTAINABILITY REPORTING 10 (2006).

⁷² *Id.*; KING & BARTELS, *supra* note 66, at 28.

⁷³ BARTELS ET AL., *supra* note 57, at 10.

⁷⁴ KPMG INT'L AND THE UNITED NATIONS ENV'T PROGRAM, *supra* note 71, at 10.

⁷⁵ Sixty percent of Global 250 companies include CSR disclosure in their annual reports. Approximately two-thirds of such companies use independent third party assurances. KING & BARTELS, *supra* note 66, at 5.

2015 KPMG Report states that integrated reporting is the exception rather than the rule.⁷⁶

A third trend relates to the content of non-financial reporting. As mentioned previously, there has been a proliferation of reporting instruments developed in recent years, yet no clear consensus has emerged on what should be reported. Some reporting frameworks cover specific environmental or social topics, while others require or encourage reporting of general sustainability information.⁷⁷ For mandatory reporting, the requirements can vary widely. The most popular frameworks for voluntary reporting among large companies have been those developed by the GRI since 1997.⁷⁸ The 2015 KPMG Report states that three-quarters of Global 250 companies use such GRI frameworks.⁷⁹ The GRI invites diverse stakeholders to participate in and lend expertise to the process of developing its frameworks.⁸⁰ Such standards incorporate widely-recognized international norms like those contained in the U.N. Global Compact and contain a set of key performance indicators on CSR issues, including human rights, anti-discrimination, labor, anti-corruption, and the environment.⁸¹ The GRI frameworks have been revised on several occasions over the years to incorporate improvements, with the GRI Standards being the most recent version.⁸²

The picture that emerges from the KPMG Reports is of ever more frequent and voluminous information being disclosed. However, such reporting may be of dubious value to stakeholders. The 2016 Carrots &

⁷⁶ Ten percent of the Global 250 companies use integrated reporting. *Id.*

⁷⁷ BARTELS ET AL., *supra* note 57, at 19.

⁷⁸ KING & BARTELS, *supra* note 66, at 42.

⁷⁹ *Id.* Such percentage has declined since 2013, when KPMG reported that 81% of Global 250 companies used the frameworks. *Id.* This was attributed to the complexity of changes to the frameworks that were introduced and the movement towards incorporating non-financial reporting in annual reports and use of integrated reporting. *Id.*

⁸⁰ BARTELS ET AL., *supra* note 57, at 25.

⁸¹ *Id.*

⁸² *Sustainability Reporting Standards*, *supra* note 11.

Sticks Report noted that the growth of sustainability reporting has resulted in “a rapidly growing, increasingly complex and fragmented landscape of reporting instruments.”⁸³ The authors called for “[a]lignment and harmonization [to] be a key goal for governments, market regulators, stock exchanges, industry associations, standard setters and all [others] responsible for developing reporting instruments.”⁸⁴ Such an effort “will require increased levels of collaboration and joint commitments” among entities developing reporting instruments, as well as among organizations that engage in such reporting.⁸⁵ The authors also advocated for steps to be taken “to prioritize and focus on the topics that are most relevant and material to the creation of long-term value both for businesses and their shareholders, and for society as a whole.”⁸⁶ Taking such steps will be challenging given the competing call for increased transparency by companies and ever more comprehensive non-financial reporting.⁸⁷ This author notes that the current situation has led to ambiguity about the content of CSR, which has created problems for governments seeking to mandate non-financial reporting.

While CSR reporting has increased significantly in recent years, there are numerous open questions surrounding such disclosure. It is unclear whether mandating such disclosure will in fact result in not just more but better reporting. Also unclear is whether the absence of a consensus around a reporting format and applicable standards will compromise the provision of consistent and comparable information that investors and other stakeholders may prefer. Perhaps the most important unanswered question is the following: How effective will the various mandates and reporting instruments prove to be in providing quality information to investors and other stakeholders that meets their demands for transparency and accountability and brings us closer to a sustainable world economy?

⁸³ BARTELS ET AL., *supra* note 57, at 22.

⁸⁴ *Id.* at 3.

⁸⁵ *Id.* at 22.

⁸⁶ *Id.*

⁸⁷ *Id.*

Section III below addresses some of these issues in the context of the 2014 EU Directive and its implementation by Member States.

III. 2014 EUROPEAN UNION DIRECTIVE ON NON-FINANCIAL REPORTING

A. Requirements of the 2014 EU Directive

This Section III.A examines the mandate of non-financial reporting set forth in the 2014 EU Directive, revealing several features that make it a weak regulatory instrument due to its limited coverage of enterprises, the flexibility given to companies to design their own disclosure approach, the lack of specific guidance on the content and framework of such reports, and the failure to set forth strong standards for third party assurances and enforcement.

European companies have long been leaders in CSR reporting. Such companies have historically reported on CSR matters at a higher rate than businesses in other parts of the world.⁸⁸ Although the Asia Pacific region has recently pulled ahead of them in terms of percentage of reporting companies, Europe still is in the forefront of non-financial reporting by business enterprises.⁸⁹

This phenomenon is fueled in part by the fact that several Member States of the EU have taken steps in recent years to mandate such reporting. This trend has accelerated as a result of the 2014 EU Directive. Pursuant to such Directive, Member States of the EU were required to enact laws requiring disclosure of non-financial information by certain large undertakings and groups by December 6, 2016.⁹⁰ Such requirements will

⁸⁸ KING & BARTELS, *supra* note 66, at 31.

⁸⁹ *Id.* (discussing the growth in corporate responsibility reporting in Asia Pacific over the West). In 2015, 79% of Asian companies produced corporate social reports in comparison to 74% of European companies. *Id.*

⁹⁰ 2014 EU Directive, *supra* note 12, at art. 4, ¶ 1 (discussing “Transposition”).

become effective for fiscal years beginning on January 1, 2017, or during calendar year 2017.⁹¹

The 2014 EU Directive, which amends EU Directive 2013/34/EU on annual financial statements, consolidated financial statements and related reports (“2013 EU Accounting Directive”), applies only to large public-interest entities (“PIEs”) with more than 500 employees (“covered PIE”).⁹² It also applies to large groups, of which a PIE is the parent entity, that meet the criterion of more than 500 employees on a consolidated basis.⁹³ The European Commission estimates that the new reporting requirements will apply to approximately 6000 entities and groups across the EU.⁹⁴

The concept of PIEs is defined in Article 2 of the 2013 EU Accounting Directive, and includes companies listed in EU markets, as well as some unlisted companies, such as credit institutions, insurance companies, and other companies that are so designated by Member States because of their activities, size or number of employees.⁹⁵ The required non-financial disclosure shall be incorporated in the PIE’s annual report.⁹⁶ However, if a covered PIE prepares a standalone CSR report for the same financial year that covers the topics required under the 2014 EU Directive, a Member State may exempt it from the requirement of including such

⁹¹ *Id.*

⁹² *Id.* at art. 1, ¶ 1 (discussing “Non-financial statement” in new Article 19a, ¶ 1).

⁹³ *Id.* at art. 1, ¶ 3 (discussing “Consolidated non-financial statement” in new Article 29a, ¶ 1).

⁹⁴ European Commission Press Release Statement/14/291, Disclosure of Non-financial Information: Europe’s Largest Companies to Be More Transparent on Social and Environmental Issues (Sept. 29, 2014).

⁹⁵ Directive 2013/34/EU, of the European Parliament and of the Council of 26 June 2013 Amending Directive 2006/43/EC of the European Parliament and of the Council and Repealing Council Directives 78/660/EEC and 83/349/EEC 2013 EU Accounting Directive On the Annual Financial statements, Consolidated Financial Statements and Related Reports of Certain Types of Undertakings, 2013 O.J. L182/19, at art. 2, ¶ 1 (discussing “Definitions”) [hereinafter 2013 EU Directive].

⁹⁶ 2014 EU Directive, *supra* note 12, at art.1, ¶ 1 (discussing “Non-financial statement” in new Article 19a, ¶ 1).

information in its annual report as long as it publishes such information along with the annual report or makes it available on the PIE's website within a reasonable time period and refers to it in the annual report.⁹⁷ This provision reflects the flexible approach towards disclosure embodied in the 2014 EU Directive in that companies who already prepare separate CSR reports based on national, international or European frameworks may continue to do so without having to change their reporting practices and duplicate such information in the annual report. This provision gives companies the flexibility to disclose non-financial information in one of two ways: either in a format that will be integrated with the annual report or in a separate standalone sustainability report.

If a covered PIE is a parent of a large group exceeding on a consolidated basis the required number of 500 employees, it shall include a consolidated non-financial statement covering the required information for the entire group.⁹⁸ However, if such parent prepares a standalone CSR report for the same financial year that covers the topics required under 2014 EU Directive, a Member State may exempt it from the requirement of including such information in its consolidated annual report as long as it publishes such information along with the consolidated annual report or makes it available on the PIE's website within a reasonable time period and refers to it in the consolidated annual report.⁹⁹ A subsidiary falling within the definition of a PIE that is part of a group does not need to file its own non-financial report if it is covered by a consolidated report filed by its parent.¹⁰⁰

The 2014 EU Directive requires disclosure of non-financial information "to the extent necessary for an understanding of the undertaking's

⁹⁷ *Id.* at art.1, ¶ 1 (discussing "Non-financial statement" in new Article 19a, ¶ 4).

⁹⁸ *Id.* at art. 1, ¶ 3 (discussing "Consolidated non-financial statement" in new Article 29a, ¶ 1).

⁹⁹ *Id.* at art. 1, ¶ 3 (discussing "Consolidated non-financial statement" in new Article 29a, ¶ 4).

¹⁰⁰ *Id.* at art.1, ¶ 1 (discussing "Non-financial statement" in new Article 19a, ¶ 3).

development, performance, position and impact of its activity.”¹⁰¹ The 2014 EU Directive states that “at a minimum” four categories of information must be covered, namely “environmental, social and employee matters, respect for human rights, anti-corruption and bribery matters.”¹⁰² These are the four areas that are most frequently the focus of CSR initiatives such as the U.N. Global Compact, as noted in Section II above.

In addition to requiring non-financial disclosure in at least these four categories, the 2014 EU Directive also requires covered companies to report on the diversity policies for their administrative, management, and supervisory bodies, regarding such factors as “age, gender, or educational and professional backgrounds.”¹⁰³ The objectives, implementation, and results for the reporting period of such policies must be included.¹⁰⁴ Diversity policies are placed in a disclosure category separate and apart from non-financial information under the 2014 EU Directive.¹⁰⁵ In addition, the policy goals of requiring such disclosure are different than the policy goals of requiring non-financial information disclosure. The stated policy goal for non-financial information disclosure in the 2014 EU directive is “managing change towards a sustainable global economy by combining long-term profitability with social justice and environmental protection” by “measuring, monitoring and managing of undertakings’ performance and their impact on society.”¹⁰⁶ The stated policy goal for disclosure of diversity policies in the 2014 EU Directive is to contribute “effective oversight of the management and to successful governance of

¹⁰¹ 2014 EU Directive, *supra* note 12, at art.1, ¶ 1 (discussing “Non-financial statement” in new Article 19a, ¶ 1).

¹⁰² *Id.* at art.1, ¶ 1 (discussing “Non-financial statement” in new Article 19a, ¶ 1).

¹⁰³ *Id.* at art. 1, ¶ 2 (discussing amendments to Article 20 of 2013 EU Directive).

¹⁰⁴ *Id.* at art. 1, ¶ 1 (discussing “Non-financial statement” under the new Article 19a, ¶ 1).

¹⁰⁵ Non-financial disclosure is covered under new Article 19a of the 2013 EU Directive relating to the non-financial information contents of the management or annual report, while diversity policies are covered under an amendment to Article 20 of the 2013 EU Directive relating to that corporate governance statement in the management or annual report. *Id.* at art. 1, ¶¶ 1, 3.

¹⁰⁶ 2014 EU Directive, *supra* note 12, at preamble, recital 3.

the undertaking” by introducing a wider variety of skills and viewpoints into management decision-making.¹⁰⁷ Because there is no clear connection between these two disclosure categories, disclosure of diversity policies will not be discussed further.

The 2014 EU Directive appears to give great latitude to the Member States on the content of non-financial disclosures. This conclusion may be drawn because the 2014 EU Directive does not spell out the content of such disclosure categories in the operative language. Rather, in the Directive’s preamble, there is a list of topics that either “should,” “may,” or “could” be disclosed for the first four categories. For environmental matters, the report “*should* contain . . . details of the current and foreseeable impacts of the undertaking’s operations on the environment, and, as appropriate, on health and safety, the use of renewable and/or non-renewable energy, greenhouse gas emissions, water use and air pollution.”¹⁰⁸ But for social and employee-related matters, the report:

[M]ay concern the actions taken to ensure gender equality, implementation of fundamental conventions of the International Labour Organisation, working conditions, social dialogue, respect for the right of workers to be informed and consulted, respect for trade union rights, health and safety at work and the dialogue with local communities, and/or the actions taken to ensure the protection and the development of those communities.¹⁰⁹

¹⁰⁷ *Id.* at preamble, recital 18

¹⁰⁸ *Id.* at preamble, recital 7 (emphasis added).

¹⁰⁹ *Id.* (emphasis added).

Finally, for human rights, anti-corruption, and anti-bribery matters, the report “*could* include information on the prevention of human rights abuses and/or on instruments in place to fight corruption and bribery.”¹¹⁰

Moreover, the 2014 EU Directive adopts a “comply or explain” approach to disclosure, meaning that companies are required to report only on issues that are covered by their policies.¹¹¹ If a company does not pursue a policy on a particular issue mandated by the 2014 EU Directive, it does not need to adopt a policy to be in compliance. It must, however, give a “clear and reasoned explanation” for why it has no policy in place.¹¹² This approach gives companies free rein to design their own approaches to non-financial reporting and to their CSR policies, subject to the requirement that they provide a reason for doing so.

There are no guidelines in the 2014 EU Directive for the format that reports should follow. However, the following elements must be reported in a company’s report: “a brief description of [its] business model;” its policies regarding the matters covered by its non-financial reporting, including its due diligence processes; “the outcomes of [such] policies;” the principal risks associated with its operations in the areas covered by such reporting, including “its business relationships, products or services which are likely to cause adverse impacts . . . and how the [company] manages [such] risks;” and the “non-financial key performance indicators relevant [for] the particular business.”¹¹³

In terms of third party assurances, non-financial information integrated in a management report will be required to be audited by the company’s auditors.¹¹⁴ Standalone sustainability reports are not required to be

¹¹⁰ *Id.* (emphasis added).

¹¹¹ 2014 EU Directive, *supra* note 12.

¹¹² *Id.* at art. 1, ¶ 1 (discussing “Non-financial statement” in new Article 19a, ¶ 1).

¹¹³ *Id.* at art. 1, ¶ 1 (discussing “Non-financial statement” in new Article 19a, ¶ 1).

¹¹⁴ *Id.* at art. 1, ¶ 1 (discussing “Non-financial statement” in new Article 19a, ¶ 5).

subject to third party assurances although individual Member States may decide to impose such a requirement.¹¹⁵

Regarding enforcement, the 2014 EU Directive states in the preamble that Member States should ensure that national procedures are in place to enforce compliance with the reporting mandate by “all persons and legal entities having a legitimate interest” in such requirements.¹¹⁶ However, such Directive does not set forth details on the types of enforcement measures that should be employed nor are minimum penalty requirements mandated.

The 2014 EU Directive takes a minimum harmonization approach to the reporting standards that can be used for non-financial disclosures. It does not contain detailed rules for the content of non-financial reporting and does not impose mandatory EU standards. It also does not require that companies use any particular CSR framework as the basis for their reporting. Instead, companies may choose to present such disclosures in the way they consider most useful.¹¹⁷ They may rely on national frameworks, EU frameworks such as the Eco-Management and Audit Scheme (EMAS), or international frameworks such as the U.N. Global Compact, the Guiding Principles on Business and Human Rights implementing the United Nations “Protect, Respect and Remedy” Framework, the Organization for Economic Co-operation and Development (OECD) Guidelines for Multinational Enterprises, the International Organization for Standardization’s ISO 26000, the International Labour Organization’s Tripartite Declaration of Principles concerning Multinational Enterprises and Social Policy, the GRI frameworks, or other recognized international frameworks.¹¹⁸

¹¹⁵ *Id.* (discussing “Non-financial statement” in new Article 19a, ¶ 6).

¹¹⁶ *Id.* at preamble, recital 10.

¹¹⁷ European Commission Consultation Document (EC) on Non-Binding Guidelines for Reporting of Non-Financial Information by Companies at 4, http://ec.europa.eu/finance/consultations/2016/non-financial-reporting-guidelines/docs/consultation-document_en.pdf. [hereinafter European Commission Consultation Document].

¹¹⁸ 2014 EU Directive, *supra* note 12, at preamble, recital 9; *see also* European Commission Consultation Document, *supra* note 117, at 4 (“Companies may also consider the sectorial

The minimum harmonization approach will probably result in companies using very different formats in their reporting, which will result in wide variations in quantity and quality of reporting. This will likely make it difficult for the users of these reports to make meaningful comparisons across companies. To mitigate this problem as well as to facilitate the disclosure of non-financial information by companies, the 2014 EU Directive required the European Commission to prepare “non-binding guidelines on methodology for reporting non-financial information, including non-financial key performance indicators, general and sectoral, with a view to facilitating relevant, useful and comparable disclosure of non-financial information by undertakings” by December 6, 2016.¹¹⁹ The European Commission conducted a public consultation that ended on April 15, 2016, in which it solicited views from stakeholders on the form that such guidance should take.¹²⁰ The topics covered in the consultation document included general principles and key attributes of non-financial information that should be addressed, such as materiality, comparability and comprehensiveness, whether the content should consist of general principles or detailed guidelines addressing specific sectoral issues, whether key performance indicators should be provided or left to the discretion of companies, whether the guidelines should relate to existing national, international or EU frameworks, and whether more clarity is needed on reporting of diversity information.¹²¹

Although the 2014 EU Directive required action by December 6, 2016, the European Commission did not issue such non-binding guidance until July 5, 2017. In its communication entitled “Guidelines on Non-

OECD Due Diligence Guidance for Responsible Supply Chains of Minerals from Conflict-Affected and High-Risk Areas, as appropriate.”).

¹¹⁹ 2014 EU Directive, *supra* note 12, at art. 2 (discussing “Guidance on reporting”).

¹²⁰ See European Commission Consultation Document, *supra* note 117; see also European Commission Press Release Statement, *European Commission Consults on Non-Binding Guidelines on Disclosure of Non-Financial Information by Certain Large Companies* (Jan. 15, 2016), <http://europa.eu/rapid/midday-express-15-01-2016.htm?locale=en#5>).

¹²¹ European Commission Consultation Document, *supra* note 117.

Financial Reporting (Methodology for Reporting Non-Financial Information)” (“2017 NFR Guidelines”), the European Commission addressed the key principles, the content, and the reporting framework for non-financial reporting under the 2014 EU Directive in the context of management reports of EU companies.¹²²

Regarding key principles, the 2017 NFR Guidelines listed (1) disclosure of material information, defined to mean “information where its omission or misstatement could reasonably be expected to influence decisions that users make on the basis of the financial statements of the undertaking;” (2) fair, balanced, and understandable reporting; (3) comprehensive yet concise disclosure encompassing at least “environmental, social and employee matters, respect for human rights, and anti-corruption and bribery matters;” (4) strategic and forward-looking disclosure of the company’s business model, strategy and its implementation, and short-term, medium-term, and long-term implications of the information; (5) stakeholder orientation addressed to “investors, workers, consumers, suppliers, customers, local communities, public authorities, vulnerable groups, social partners and civil society;” and (6) non-financial reporting that is clearly linked with and forms a coherent whole with other elements of the management report, with content that is consistent over time to allow comparability among time periods, and is consistent in its choice of key performance indicators.¹²³

Regarding content, the 2017 NFR Guidelines listed examples of material information to be included in non-financial reporting and management reports in each of the categories mandated by the 2014 EU Directive. These categories included (1) “a brief description of the undertaking’s business model;” (2) “a description of the policies pursued by the undertaking in relation to those matters, including due diligence processes

¹²² See Communication from the European Commission (EC), Guidelines on Non-Financial Reporting (Methodology for Reporting Non-Financial Information), 60/2017 of 5 July 2017, 2017 O.J. (C 215) [hereinafter 2017 NFR Guidelines].

¹²³ *Id.* § 3.

implemented;” (3) “the outcome of [such] policies;” (4) relevant risks relating to business operations in these areas and how such risks are managed; (5) non-financial key performance indicators relevant to the business; and (6) thematic aspects of the minimum content areas of non-financial information mandated by the 2014 EU Directive, namely environmental, social, and employee matters, respect for human rights, and anti-corruption and anti-bribery matters.¹²⁴ For each of these content areas, the 2017 NFR Guidelines provide examples of material information that companies could consider disclosing, along with related key performance indicators.¹²⁵

Regarding reporting frameworks, the 2017 NFR Guidelines restate language from the 2014 EU Directive giving companies the flexibility to use “high quality, broadly recognised national, EU-based or international frameworks”¹²⁶ Such Guidelines set forth examples of EU-based frameworks such as the Eco-Management and Audit Scheme (EMAS) and international frameworks such as the U.N. Global Compact, the Guiding Principles on Business and Human Rights implementing the United Nations “Protect, Respect and Remedy” Framework, the Organization for Economic Co-operation and Development (OECD) Guidelines for Multinational Enterprises, the International Organization for Standardization’s ISO 26000, the International Labour Organization’s Tripartite Declaration of Principles concerning Multinational Enterprises and Social Policy, and the GRI frameworks, and also refers to a list of some twenty frameworks set forth at the beginning of the Guidelines.¹²⁷ The 2017 NFR Guidelines do not prioritize these frameworks or provide any guidance on which, if any, of these reporting frameworks is recommended. In fact, the Guidelines note that the list provided is not exhaustive and there may be additional frameworks that can be used for non-financial

¹²⁴ *Id.* § 4.

¹²⁵ *Id.* §§ 3.2, 4.5.

¹²⁶ *Id.* § 5.

¹²⁷ 2017 NFR Guidelines, *supra* note 122, § 5.

reporting. The Guidelines suggest that, for purposes of “clarity and comparability,” a company relying on one or several of these frameworks should disclose which frameworks it has used for specific disclosures.¹²⁸

While the 2017 NFR Guidelines provide some additional guidance on the non-financial reporting mandate set forth in the 2014 EU Directive, they fail to provide clear guidance on the contents and reporting framework that will be most informative to stakeholders seeking to utilize such non-financial information. As a result, they fail to address the concern that the 2014 EU Directive does not facilitate comparability and consistency in non-financial reporting across the EU companies covered by the Directive.

B. Policy Objectives and Historical Development of the 2014 EU Directive

This Section III.B explores the development of EU policy and legislation on non-financial reporting that resulted in the adoption of the 2014 EU Directive. Through a series of steps taken over the time period from 2001 through 2014, the European Commission articulated a clear vision for enhanced transparency on CSR and an increasingly detailed agenda for achieving that result. Such agenda sought to engage the business community by emphasizing the benefits projected to result from non-financial reporting and situating companies at the center of the disclosure process, while carving out a new but somewhat limited role for government regulation. The resulting “smart mix approach” allows both the public and the private sectors to play a role and thus is an improvement over a purely voluntary approach to non-financial reporting. However, reluctance on the part of the business community to accept stronger standards for such reporting may hinder the policy objectives of the 2014 EU Directive from being achieved in the near term.

The policy goal of the 2014 EU Directive was to introduce greater information transparency in non-financial matters by EU companies. The EU has touted the economic benefits of this policy, namely the belief that

¹²⁸ *Id.*

companies, investors, and society at large will benefit from increased transparency because it leads to stronger long-term performance, which is important for Europe's long-term competitiveness and the creation of jobs.¹²⁹ It is the latest step taken towards this goal by the EU in what appears to be an evolutionary process with its origins in the early 1990s.¹³⁰ However, the 2014 EU Directive must be viewed only as an intermediate step that will require further refinement if the policy goal is to be achieved.

In tracing the history of the development of non-financial reporting in the EU, four major policy themes emerge: (1) the value of non-financial information transparency and the potential benefits it offers to business; (2) the importance of key stakeholder engagement with CSR issues, including with consumers, employees, and investors; (3) the emergence of a role for government regulation that complements voluntary initiatives by business; and (4) the need for convergence around a common set of reporting standards. These themes have been repeated in both legislative enactments and policy statements issued by various EU institutions.

Starting with the 2014 EU Directive, such Directive states its primary policy objective as improving the “transparency of the social and environmental information provided by undertakings in all sectors.”¹³¹ The Directive notes that this is a “continuous endeavour,” recognizing that improving transparency may be a process that takes place through a series of steps over time.¹³² Other policy objectives mentioned in the lan-

¹²⁹ European Commission Consultation Survey (EC), Public Consultation on Non-Binding Guidelines on Methodology for Reporting Non-financial Information (Apr. 14, 2016), <http://www.eumedion.nl/en/public/knowledgenetwork/consultations/2016-04-eusurvey---non-binding-non-financial-information-guidelines.pdf>.

¹³⁰ See *European Commission Green Paper on Promoting a European Framework for Corporate Social Responsibility*, COM (2001) 366 final (July 18, 2001), <http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52001DC0366&from=EN> [hereinafter 2001 Green Paper]; see also Kinderman, *supra* note 20, at 716.

¹³¹ 2014 EU Directive, *supra* note 12, at preamble, recital 1.

¹³² *Id.*

guage of the Directive include enhancing “the consistency and comparability of non-financial information disclosed throughout the Union”¹³³ and “coordination of national provisions concerning the disclosure of non-financial information in respect of certain large undertakings . . . [which] is necessary . . . because most of those undertakings operate in more than one Member State.”¹³⁴

The rationales for seeking to promote improved transparency set forth in the 2014 EU Directive include “identifying sustainability risks,” “increasing investor and consumer trust,” and “managing change towards a sustainable global economy by combining long-term profitability with social justice and environmental protection.”¹³⁵ Disclosure is said to help “the measuring, monitoring and managing of undertakings’ performance and their impact on society.”¹³⁶

Looking further back in time, the 2001 Green Paper on Promoting a European Framework for Corporate Social Responsibility (“2001 Green Paper”) represented the European Commission’s first attempt to develop a CSR policy for the EU.¹³⁷ The purpose of the 2001 Green Paper was to promote a discussion on advancing CSR in Europe and on the international level, with a focus on innovation, transparency, and deepening partnerships with stakeholders.¹³⁸

In the 2001 Green Paper, the European Commission sets forth several fundamental principles underlying CSR, including a definition of CSR that reads as follows: “a concept whereby companies integrate social and environmental concerns in their business operations and in their interaction with their stakeholders on a voluntary basis.”¹³⁹ The 2001 Green

¹³³ *Id.* at preamble, recital 6.

¹³⁴ *Id.* at preamble, recital 4.

¹³⁵ *Id.* at preamble, recital 3.

¹³⁶ *Id.*

¹³⁷ See 2001 Green Paper, *supra* note 130.

¹³⁸ *Id.* at 3 (discussing “Executive Summary” at ¶ 7).

¹³⁹ *Id.* at 6 (discussing “What is corporate social responsibility?” at ¶ 20).

Paper stated that CSR meant “going beyond compliance and investing ‘more’ into human capital, the environment and the relations with stakeholders.”¹⁴⁰

The 2001 Green Paper emphasized the “business case” for CSR broadly defined.¹⁴¹ It explicitly linked CSR with the notion of sustainable business practices and thus focused on a long-term strategy connecting economic growth, social cohesion, and environmental protection.¹⁴² It identified both direct and indirect economic benefits that flowed from CSR and produced “better performance” and “more profits and growth.”¹⁴³ These included a better working environment leading to a more productive work force, more efficient use of natural resources, and more attention from consumers and investors leading to increased market opportunities.¹⁴⁴

In addition to setting forth a definition and supporting principles for CSR, the 2001 Green Paper discussed trends in CSR that were current at the time, including the development of CSR reporting in Europe. On that topic, the Green Paper noted that while it is businesses that must become socially responsible, other stakeholders including employees, consumers, and investors can prompt business to adopt responsible practices.¹⁴⁵ Transparency about the social and environmental performance of business is key to that process.¹⁴⁶

¹⁴⁰ *Id.* at 6 (discussing “What is corporate social responsibility?” at ¶ 21).

¹⁴¹ *Id.* at 4, 22. The business case for CSR is discussed *supra* Section II. David Vogel has noted that a belief in the business benefits of CSR is particularly influential in Europe. Vogel, *Is There a Market for Virtue?*, *supra* note 33.

¹⁴² 2001 Green Paper, *supra* note 130, at 4 (discussing “Introduction” at ¶ 9).

¹⁴³ *Id.* at 7 (discussing “What is corporate social responsibility?” at ¶ 24).

¹⁴⁴ *Id.*

¹⁴⁵ *Id.* at 15 (discussing “A holistic approach towards corporate social responsibility” at ¶ 62).

¹⁴⁶ *Id.*

The 2001 Green Paper noted some of the problems associated with existing CSR reporting, especially lack of consistency in content, reporting format, and use of reliability and audit standards.¹⁴⁷ It described the proliferation of public and private initiatives in support of social and environmental reporting that had been taken at the national and international level, and the wide variety of approaches and lack of coherence among such standards.¹⁴⁸ However, it noted the emergence of the GRI Guidelines as evidence of best practices on the environmental side.¹⁴⁹

In an attempt to engage stakeholders, the 2001 Green Paper launched a public consultation process ending on December 31, 2001, in which the European Commission posed eighteen questions on which it sought stakeholder input.¹⁵⁰ The results of the consultation were announced in a 2002 European Commission communication entitled “Corporate Social Responsibility: A business contribution to Sustainable Development” (“2002 EC Communication”).¹⁵¹ Such communication set forth a “European Action Framework for CSR,” which included “facilitating convergence and transparency of CSR practices and tools.”¹⁵² The European Commission once again noted the proliferation of CSR initiatives, which differed in scope and applicability to various businesses, sectors or industries, and their inability to meet the needs for transparency of business performance.¹⁵³ For that reason, the 2002 EC Communication called for “a certain convergence of concepts, instruments, practices, which would increase transparency without stifling innovation, and would

¹⁴⁷ 2001 Green Paper, *supra* note 130, at 16 (discussing “Social responsibility reporting and auditing” at ¶ 66).

¹⁴⁸ *Id.* at 17 (discussing “Social responsibility reporting and auditing” at ¶ 71).

¹⁴⁹ *Id.*

¹⁵⁰ *Id.* at 21–23 (discussing “The consultation process” at ¶ 92).

¹⁵¹ *European Commission Communication on Corporate Social Responsibility: A Business Contribution to Sustainable Development*, COM (2002) 347 final (July 2, 2002) [hereinafter 2002 EC Communication].

¹⁵² *Id.* at 5, 8.

¹⁵³ *Id.* at 13.

offer benefits to all parties . . . [and] build upon core values and take their starting point in international agreed instruments”¹⁵⁴

Another important feature of the 2002 EC Communication was the establishment of an EU multi-stakeholder forum on CSR (“EMS Forum”).¹⁵⁵ The purpose of the EMS Forum, which was launched on October 16, 2002, was to facilitate dialogue among businesses and their stakeholders, including employers, employees, consumers, and civil society, as well as professional associations and business networks, with the aim of “promoting transparency and convergence of CSR practices and instruments.”¹⁵⁶ The EMS Forum issued a final report in June 2004.¹⁵⁷ After that date, it continued to meet and work on CSR issues on several occasions.¹⁵⁸

In a later European Commission Communication from 2006 entitled “Implementing the Partnership for Growth and Jobs: Making Europe a Pole of Excellence on Corporate Social Responsibility” (“2006 EC Communication”), the European Commission noted that progress had been made on awareness, understanding, and uptake of CSR as a result of

¹⁵⁴ *Id.*

¹⁵⁵ *Id.* at 17.

¹⁵⁶ 2002 EC Communication, *supra* note 151, at 17.

¹⁵⁷ *European Commission Communication on Implementing the Partnership for Growth and Jobs: Making Europe a Pole of Excellence on Corporate Social Responsibility*, at 3, COM (2006) 136 final (Mar. 22, 2006) [hereinafter 2006 EC Communication].

¹⁵⁸ *EU Multi Stakeholder Forum on CSR: Next Steps*, EURACTIV (Jan. 12, 2003), <http://www.euractiv.com/section/social-europe-jobs/news/eu-multi-stakeholder-forum-on-csr-next-steps/>; *Executive Summary: EU Multi Stakeholder Forum on Corporate Social Responsibility*, (Feb. 3–4, 2015), <http://ec.europa.eu/DocsRoom/documents/8774/attachments/1/translations/en/renditions/native>.

the EMS Forum, including a consensus that arose around the Commission's definition of CSR.¹⁵⁹ However, no consensus was achieved on topics such as company reporting requirements and the need for a European standard for CSR.¹⁶⁰

The European Commission acknowledged that more involvement by business was needed and invited enterprises to strengthen their commitment to CSR by joining a newly instituted "European Alliance for CSR."¹⁶¹ The European Commission described this initiative as a "partnership" built on the understanding that CSR can contribute to sustainable development and enhance European business innovation and competitiveness, all of which will lead to economic growth and job creation.¹⁶² In such a partnership, business was to take the lead and the role of the European Commission was to play a supporting or facilitating role by promoting the voluntary and innovative CSR practices of business and by encouraging and disseminating good practices.¹⁶³ One commentator has interpreted the creation of the European Alliance for CSR as a move by the European Commission "to outsource policy on CSR to business."¹⁶⁴ The key areas for EU action announced in the 2006 EC Communication included "[a]wareness-raising and best practice exchange," "[s]upport to multi-stakeholder initiatives," "[c]ooperation with Member States," "[c]onsumer information and transparency," "[r]esearch," "[e]ducation," small and medium-sized enterprises ("SMEs"), and "[t]he international dimension of CSR."¹⁶⁵

¹⁵⁹ 2006 EC Communication, *supra* note 157, at 3.

¹⁶⁰ *Id.*

¹⁶¹ *Id.* at 3.

¹⁶² European Commission Press Release IP/06/358, Launch of "European Alliance for Corporate Social Responsibility" (Mar. 22, 2006), at 4.

¹⁶³ *Id.* at 6.

¹⁶⁴ Kinderman, *supra* note 20, at 716.

¹⁶⁵ 2006 EC Communication, *supra* note 157, at 6–8.

In terms of EU legislative action, the first mention of non-financial reporting was in the 2003 Accounts Modernization Directive, EU Directive 2003/51/EC (“2003 EU Directive”), which required enterprises to disclose in their annual reports “[t]o the extent necessary for an understanding of the company's development, performance or position, . . . both financial and, where appropriate, non-financial key performance indicators relevant to the particular business, including information relating to environmental and employee matters.”¹⁶⁶ In addition, such Directive contained language that allowed Member States to exempt SMEs from such non-financial reporting requirement, and all Member States have chosen to do so.¹⁶⁷ Due to its conditional language (“to the extent necessary” and “where appropriate”), the 2003 EU Directive cannot be viewed as containing a mandate for non-financial reporting. The carve-out for SMEs also limited the effectiveness of the 2003 EU Directive in promoting enhanced non-financial reporting.

The 2003 EU Directive remained the only legislation on non-financial reporting that was in place until adoption of the 2014 EU Directive. The 2014 EU Directive was the culmination of a series of additional steps taken by EU institutions to refine CSR principles, including those relating to non-financial reporting.

In 2011, the European Commission announced the development of a renewed strategy for CSR in a communication entitled “A renewed EU strategy 2011-2014 for Corporate Social Responsibility” (“2011 CSR

¹⁶⁶ Directive 2003/51/EC of the European Parliament and of the Council of 18 June 2003 amending Directives 78/660/EEC, 83/349/EEC, 86/635/EEC and 91/674/EEC on the annual and consolidated accounts of certain types of companies, banks and other financial institutions and insurance undertakings (commonly known as the Fourth Company Law Directive), 2003 O.J. L 178/18, at art. 1, ¶ 14(a), (b) [hereinafter 2003 EU Directive].

¹⁶⁷ *Id.* at art. 1 ¶ 14(b) (amending Article 46 of Directive 78/660/EEC); *see also European Commission Communication on A Renewed EU Strategy 2011-14 for Corporate Social Responsibility*, at 11 fn. 21, COM (2011) 681 final (Oct. 25, 2011) [hereinafter 2011 CSR Strategy].

Strategy”).¹⁶⁸ The European Commission had been requested to take action by the European Council and the European Parliament to further develop CSR policy.¹⁶⁹ Although the European Commission acknowledged some progress on CSR issues since the publication of the 2001 Green Paper, it also recognized that “important challenges remain[ed]”.¹⁷⁰ These included failure of European companies to integrate “social and environmental concerns into their operations and core strateg[ies],” and lack of adoption of national CSR policy frameworks by nearly half of EU Member States.¹⁷¹ Once again, the European Commission emphasized the “business case” for CSR, speaking of the benefits that a “strategic approach to CSR” could bring to the competitiveness of enterprises “in terms of risk management, cost savings, access to capital, customer relationships, human resource management, and innovation capacity.”¹⁷²

Two significant changes to EU CSR policy emerged from the 2011 CSR Strategy. First, it redefined CSR as “the responsibility of enterprises for their impacts on society.”¹⁷³ This is a broadening of the earlier definition, which referred only to environmental and employee issues and used tentative language about company non-financial disclosure (“to the extent necessary”), which could be understood to allow companies to integrate such issues in business operations on a voluntary basis. Under the revised definition, enterprises are now to be held responsible for all of their impacts. In order to fulfill such responsibilities, businesses will need to have

¹⁶⁸ 2011 CSR Strategy, *supra* note 167, at 4.

¹⁶⁹ *Id.* (citing European Council and European Parliament action in Environment Council 5 Dec. 2008, Environment Council 20 Dec. 2010, Foreign Affairs Council 14 June 2010, European Parliament Resolution 13 Mar. 2007 (P6_TA(2007)0062), European Parliament Resolution 8 June 2011 P7_TA(2011)0260).

¹⁷⁰ *Id.* at 5.

¹⁷¹ *Id.*

¹⁷² *Id.* at 3.

¹⁷³ 2011 CSR Strategy, *supra* note 167, at 6.

a process for integrating CSR into their business operations and core strategies.¹⁷⁴

A second significant change was the role assigned to government in CSR. Rather than referring to CSR as a voluntary initiative on the part of business, which was the traditional view of CSR, the 2011 CSR Strategy stated that government should play a supporting role through “a smart mix of voluntary policy measures and, where necessary, complementary regulation, for example to promote transparency, create market incentives for responsible business conduct, and ensure corporate accountability.”¹⁷⁵ The mention of use of regulation to promote transparency foreshadowed the non-financial reporting requirements of the 2014 EU Directive.

The 2011 CSR Strategy set forth an eight point action agenda, which included enhancing the visibility of CSR and disseminating good practices; improving and tracking levels of trust in business; improving self-regulation and co-regulation processes such as codes of conduct; strengthening market incentives for CSR; improving company disclosure of social and environmental information; further integrating CSR into education, training, and research; emphasizing the importance of national and sub-national CSR policies; and better aligning European and global approaches to CSR.¹⁷⁶

The fifth action item on the eight point agenda, namely improving company disclosure of social and environmental information, revealed the European Commission’s concern with the fact that only a small percentage of European companies, approximately 2,500 out of a total of 42,000

¹⁷⁴ *Id.*

¹⁷⁵ *Id.* at 7. “Enterprises must be given the flexibility to innovate and to develop an approach to CSR that is appropriate to their circumstances. Many enterprises nevertheless value the existence of principles and guidelines that are supported by public authorities, to benchmark their own policies and performance, and to promote a more level playing field.” *Id.*

¹⁷⁶ *Id.* at 8–15.

large companies operating in the EU, published CSR reports.¹⁷⁷ The European Commission also noted its concern with differences among national standards on non-financial disclosure that could create additional costs for enterprises operating in more than one Member State.¹⁷⁸ The 2011 CSR Strategy envisioned preparation of a legislative proposal on the transparency of the social and environmental information provided by companies in all sectors.¹⁷⁹

As a result of the 2011 CSR Strategy, the EU adopted stronger non-financial reporting requirements in the 2014 EU Directive. As detailed in the 2013 European Commission proposal for a new directive to improve the transparency of social and environmental information by EU companies (“2013 EU Proposal”), the EU took a series of steps in developing such proposal, consisting of careful analysis of the issues involved.¹⁸⁰ Such steps included regular dialogue with stakeholders, including through use of public consultations, eliciting expert group opinions, and meeting with stakeholders and Member States’ representatives.¹⁸¹ The European Commission also hired an external consultant to study non-financial reporting practices based on published EU company reports and to conduct a cost-benefit analysis of non-financial reports.¹⁸² In addition, the European Commission completed an impact assessment that accompanied the 2013 EU Proposal, in which it analyzed various policy options

¹⁷⁷ *Id.* at 11.

¹⁷⁸ 2011 CSR Strategy, *supra* note 167, at 11.

¹⁷⁹ *Id.* at 12.

¹⁸⁰ See *European Commission Proposal for a Directive of the European Parliament and of the Council amending Council Directive 78/660/EEC and 83/349/EEC as regards disclosure of non-financial and diversity information by certain large companies and groups*, COM (2013) 207 final (Apr. 16, 2013) [hereinafter 2013 EU Proposal].

¹⁸¹ *Id.* at ¶ 2.

¹⁸² See Final Report on the Disclosure of non-financial information by Companies, Centre for Strategy and Evaluation Services, (Dec. 2011), http://ec.europa.eu/internal_market/accounting/docs/non-financial-reporting/com_2013_207-study_en.pdf.

and then recommended a legislative approach (“2013 EU Impact Assessment”).¹⁸³

The 2013 EU Impact Assessment, which accompanied and was echoed in the 2013 EU Proposal, identified the issues of inadequate transparency of non-financial information and lack of board diversity.¹⁸⁴ Regarding lack of transparency of non-financial information, which is the focus of this article, both the low quantity and the poor quality of reporting were noted.¹⁸⁵ The European Commission attributed the problem to both market failure and regulatory failure.¹⁸⁶ Regarding market failure, the European Commission noted that market incentives seemed insufficient because the benefits appear long-term and uncertain to market participants while the short-term costs appear high and easily quantifiable.¹⁸⁷ Regarding regulatory failure, it noted that the 2003 Accounting Directive fails to provide a clear legal obligation, leading most companies to view non-financial reporting as voluntary under such Directive.¹⁸⁸ Although some Member States had enacted legislation that exceeded the obligations of the 2003 Accounting Directive, such laws varied widely in content and scope, leading to difficulties for analysts and investors seeking to compare or benchmark companies across the EU.¹⁸⁹ Such lack of transparency was deemed to negatively impact both the companies that prepare such information as well as the users of such information, including investors, non-

¹⁸³ European Commission Staff Working Document Impact Assessment Accompanying the Document Proposal for a Directive of the European Parliament and of the Council amending Council Directive 78/660/EEC and 83/349/EEC as regards Disclosure of Non-financial and Diversity Information by Certain Large Companies and Groups, SWD (2013) 127 final (Apr. 16, 2013) [hereinafter 2013 EU Impact Assessment].

¹⁸⁴ *Id.* at 8. As mentioned previously, this article will discuss only the first issue of transparency of non-financial information.

¹⁸⁵ *Id.* at 10–11.

¹⁸⁶ *Id.* at 11–12.

¹⁸⁷ *Id.*

¹⁸⁸ 2013 EU Impact Assessment, *supra* note 183, at 12.

¹⁸⁹ *Id.* at 23, 38, 44.

governmental organizations, and public authorities.¹⁹⁰ Negative impacts were noted in the areas of company performance (due to management's failure to integrate non-financial risks and opportunities into business operations and strategies), accountability (due to failure of companies to meet the non-financial information demands of civil society), and capital market efficiency (due to lack of integration of non-financial considerations into investor decision-making processes).¹⁹¹

In the 2013 EU Impact Assessment, the European Commission noted that, although there was non-binding guidance for non-financial reporting that had been developed at the international level, there was no global standard setter that would advance the cause of non-financial reporting in the short-term.¹⁹² Moreover, the principle of subsidiarity gives the EU the authority to act if it could achieve better results than the Member States, subject to the proviso that its action is limited to what is necessary to achieve the objectives and complies with the principle of proportionality.¹⁹³ Since the European Commission believed that it was preferable to legislate through EU law, it chose to take action to strengthen the non-financial reporting requirements for EU companies.

The 2013 EU Impact Assessment contained a list of policy options to address the need for greater non-financial information disclosure. These included no change in existing law (Option 0); requiring a statement on non-financial information in the company annual report based on a set of minimum disclosure standards (Option 1); requiring detailed reporting in a standalone non-financial report prepared in accordance with international frameworks and the use of key performance indicators (Option 2), either on a mandatory (Option 2a), report or explain (Option 2b), or voluntary basis (Option 2c); or setting up a mandatory EU reporting standard

¹⁹⁰ *Id.* at 13.

¹⁹¹ *Id.*

¹⁹² *Id.* at 21.

¹⁹³ 2013 EU Impact Assessment, *supra* note 183, at 22.

(Option 3).¹⁹⁴ The 2013 EU Impact Assessment also contained a detailed examination of each of the policy options, including a cost-benefit analysis that delved into the effectiveness in increasing the quantity and quality of information, the efficiency or compliance cost, the impact on competitiveness, and the coherence with EU legislation of each of the policy options.¹⁹⁵ The European Commission concluded, based on such analysis that the preferred policy option would be what it termed a “smart mix” of a mandatory statement in the annual report (Option 1) and a voluntary detailed standalone report (Option 2c).¹⁹⁶ Under such preferred policy option, companies would be required to include a statement containing material non-financial information in their annual reports, subject to a report or explain standard if they lacked a policy in any required disclosure area and also subject to an exemption if they prepared a detailed standalone report on a voluntary basis.¹⁹⁷

The 2013 EU Proposal and the accompanying 2013 EU Impact Assessment ultimately resulted in the adoption of the 2014 EU Directive by the European Parliament and the Council of the European Union. Due to opposition from the business community to some of the proposed wording, the 2014 EU Directive differed in several respects from the 2013

¹⁹⁴ *Id.* at 25–26.

¹⁹⁵ *Id.* at 27–30.

¹⁹⁶ *Id.* at 30.

¹⁹⁷ *Id.* (“Companies would be required to disclose material non-financial information in the form of a statement in their Annual Report. Those companies that do not have a specific policy in one or more topical areas would be at least required to explain why this is the case. For companies willing to prepare a detailed report on a voluntary basis, the proposed policy mix would provide an exemption from the disclosure obligation described under Option 1, provided that: (i) the report covers the same topics and content, (ii) it makes reference to international frameworks, and (iii) it is included in the Annual Report. This provision builds on existing practices and provides a limited but useful incentive to improve the quality of those reports. Information would be disclosed in reference to high quality, generally accepted international frameworks, and verified for consistency due to the inclusion in the Annual Report.”).

EU Proposal.¹⁹⁸ The 2013 EU Proposal was drafted to cover companies with over 500 employees and was estimated to apply to 18,000 companies, but the scope of the 2014 EU Directive was narrowed to apply only to PIEs of over 500 employees such as public companies and financial institutions, resulting in a reduced estimate of only 6,000 covered companies.¹⁹⁹ In addition, the 2013 EU Proposal provided that companies publishing standalone non-financial information reports incorporate such documents in their annual reports, while the 2014 EU Directive allows companies to make such information publicly available on the company website within a reasonable time period not to exceed six months as long as this is referenced in the annual report.²⁰⁰ Another change to the 2013 EU Proposal was inclusion of a carve-out for sensitive information that, in the opinion of the company, would seriously compromise its commercial position.²⁰¹ Such changes weakened the 2014 EU Directive as it was ultimately adopted.

C. Implementation of the 2014 EU Directive

The 2014 EU Directive required Member States to inform the European Commission of the entry into force of laws, regulations, and administrative provisions needed to comply by December 6, 2016.²⁰² Pursuant to such Directive, Member States may enact laws with higher requirements, but may not choose to implement a lower level of reporting.²⁰³

¹⁹⁸ See Daniel Kinderman, *The Struggle over the EU Non-financial Disclosure Directive*, 8/2015 WSI-MITTEILUNGEN 613, 613–21 (2015), http://www.boeckler.de/wsi-mitteilungen_62503_62549.htm (available in English at <https://ssrn.com/abstract=2614983>).

¹⁹⁹ 2013 EU Proposal, *supra* note 180, ¶ 1.

²⁰⁰ *Id.*

²⁰¹ *Id.*

²⁰² 2014 EU Directive, *supra* note 12, at art. 4, ¶ 1 (discussing “Transposition”).

²⁰³ *Id.* at preamble, recital 1. The European Commission had previously identified that requiring this type of uniformity throughout the Member States is “fully consistent with the possibility for Member States to require, as appropriate, further improvements to the transparency of undertakings’ non-financial information.” *Id.*

In spite of the firm deadline, not all Member States submitted timely notifications and not all submissions fully complied with the 2014 EU Directive by such date.²⁰⁴

Prior to the 2014 EU Directive, a number of Member States had already implemented non-financial reporting requirements.²⁰⁵ These jurisdictions include France, Denmark, the United Kingdom, Spain, Italy, Finland, Portugal and Sweden.²⁰⁶ For Member States with pre-existing laws, amendments to such laws were required if they did not conform to the minimum requirements set out in the Directive. For Member States that did not require such reporting prior to 2014, new laws had to be enacted.

According to the 2015 KPMG Report, the four European countries with the highest rates of CSR reporting in annual reports are France, the United Kingdom, Norway, and Denmark.²⁰⁷ This Section III.C will examine the laws relating to non-financial reporting in two of these countries, France and Denmark, as examples of the types of laws that Member States with a demonstrated commitment to fostering such reporting had put in place prior to the 2014 EU Directive.²⁰⁸ It also will discuss the need

²⁰⁴ European Commission, Non-financial reporting directive – transposition status, https://ec.europa.eu/info/publications/non-financial-reporting-directive-transposition-status_en. In those cases, the 2014 EU Directive is directly applied in such Member States.

²⁰⁵ The 28 EU Member States are Austria, Belgium, Bulgaria, Croatia, Republic of Cyprus, Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Latvia, Lithuania, Luxembourg, Malta, Netherlands, Poland, Portugal, Romania, Slovakia, Slovenia, Spain, Sweden and the UK, https://europa.eu/european-union/about-eu/countries_en?country=PL.

²⁰⁶ Chris Hibbitt & David Collison, *Corporate Environmental Disclosure and Reporting Developments in Europe*, 24(1) SOC. AND ENVTL. ACCOUNTABILITY J. 1 (2004).

²⁰⁷ KING & BARTELS, *supra* note 66, at 37 (discussing countries with the highest rate of corporate responsibility reporting in annual reports).

²⁰⁸ While the United Kingdom has taken steps to promote non-financial reporting and to implement the 2014 EU Directive, this Section III.C will not cover United Kingdom legislative developments. This is due to the fact that the United Kingdom is taking steps to exit the EU, so-called “Brexit.” Stephen Castle, *U.K. Initiates ‘Brexit’ and Wades Into a Thorny Thicket*, N.Y. TIMES (Mar. 29, 2017), <https://www.nytimes.com/2017/03/29/world/europe/brexit-uk-eu-article-50.html>. For further insight into the history of non-financial reporting initiatives in the United Kingdom, see Cynthia A. Williams &

to amend such pre-existing laws in these countries in order to implement the 2014 EU Directive.

The implementation case studies in these two Member States illustrate three important points. First, the development of non-financial reporting practices is an evolutionary process that may take years to accomplish as countries adapt to new and changing circumstances pertaining to such reporting. Second, the trajectory of legislative developments in these two Member States resulted in unique national laws, yet there are some similarities, including maintaining a strong role for business decision-making, such as by allowing companies to “comply or explain” with respect to the disclosure of CSR policies (France) or to simply explain that no policy is in place (Denmark). Third, even for countries that have been leaders in mandating such reporting through legislation, the process of implementing the 2014 EU Directive has required additional legislative changes to conform to the requirements of such Directive. The process of implementation will prove even more challenging for EU Member States that did not have legislation in place prior to the 2014 EU Directive.

1. France

France has been a leader in promoting CSR reporting. It was the first country in the EU to require CSR reporting for companies whose shares are listed on an exchange, even before the EU took steps to encourage non-financial reporting in 2003.²⁰⁹ It was also the first country to mandate that such reporting be included in management’s annual report alongside financial reporting.²¹⁰

John M. Conley, *Triumph or Tragedy? The Curious Path of Corporate Disclosure Reform in the U.K.*, 31 WM. & MARY ENVTL. L. & POL’Y REV. 317 (2007).

²⁰⁹ République Française, *Preparatory Document for the French National Plan for the Development of Corporate Social Responsibility (CSR)*, 11 (2013), http://www.diplomatie.gouv.fr/en/IMG/pdf/PREPARATORY_DOCUMENT_FOR_THE_FRENCH_NATIONAL_PLAN_FOR_THE_DEVELOPMENT_OF_CORPORATE_SOCIAL_RESPONSIBILITY_CSR_.pdf.

²¹⁰ *Id.*

The French law on non-financial reporting has been on the books since 2001 when Article 116 of *Les Nouvelles Régulations Economiques* (“NRE”), the Law on New Economic Regulations, amending Article 225-102-1 of the French Commercial Code, was adopted (such law as amended hereinafter referred to as “French NFR Law”).²¹¹ Article 116 was implemented through a 2002 decree of the *Conseil d’Etat*, the Council of State (“2002 Decree”).²¹²

The purpose of the law was to increase transparency and allow shareholders and other stakeholders, including rating agencies, to better assess company performance.²¹³ While some of the information required to be disclosed was already being collected by companies, the new law expanded both the categories of information that needed to be addressed and the depth of analysis to be provided.²¹⁴ Another new feature was the fact that such information became publicly available for the first time. Previously, only management, and in some cases employees in Works Councils, had access to the information.²¹⁵

²¹¹ See Loi 2001-420 du 15 mai 2001 relative aux nouvelles régulations économiques [Law 2001-420 of May 15, 2001 Relating to French New Economic Regulations Act], JOURNAL OFFICIEL DE LA RÉPUBLIQUE FRANÇAISE [J.O.] [OFFICIAL GAZETTE OF FRANCE], May 15, 2001, p. 7776.

²¹² Décret 2002-221 du 20 février 2002 pris pour l'application de l'article L. 225-102-1 du code de commerce et modifiant le décret n° 67-236 du 23 mars 1967 sur les sociétés commerciales [Decree 2002-221 of February 20, 2002 Taken for the Application of Article L. 225-102-1 of the Commercial Code and Amending Decree 67-236 of March 23, 1967 on Commercial Companies] JOURNAL OFFICIEL DE LA RÉPUBLIQUE FRANÇAISE [J.O.] [OFFICIAL GAZETTE OF FRANCE], Feb. 20, 2002, p. 3360.

²¹³ Ministère des Affaires Etrangères – France: Office of the Ambassador At Large for Corporate Social Responsibility, *The French Legislation on Extra-Financial Reporting: Built on Consensus*, 1 (Dec. 2012),

http://www.diplomatie.gouv.fr/en/IMG/pdf/Mandatory_reporting_built_on_consensus_in_France.pdf.

²¹⁴ Mary Lou Egan et al., *France’s Nouvelles Régulations Economiques: Using Government Mandates for Corporate Reporting to Promote Environmentally Sustainable Economic Development*, at 12–13 (unpublished manuscript) (2003), <http://www.bendickegan.com/pdf/EganMauleonWolffBendick.pdf>.

²¹⁵ *Id.* at 12.

In response to perceived deficiencies in Article 116 of the NRE legislation and the 2002 Decree, Article 225 of the Grenelle II Law of July 12, 2010 was enacted.²¹⁶ This law builds on the non-financial reporting mechanism established under the NRE by once again amending Article 225-102-1 of the French Commercial Code. Such provision was implemented through a decree published on April 26, 2012 (“2012 Decree”).²¹⁷

An examination of the history of the French NFR Law reveals that non-financial reporting in France builds on a stakeholder consensus in favor of such reporting and has evolved gradually over a decade or more. Companies that are covered by such law include publicly listed companies and other large companies as defined in the legislation, namely unlisted companies with over 500 employees and a balance sheet total or net turnover exceeding EUR 100 million. This latter category of large unlisted companies was added pursuant to the 2012 Decree and became effective after December 31, 2013.

Such covered companies must provide certain quantitative and qualitative non-financial information in their annual reports. The French NFR Law provides a list of required categories of disclosure that has expanded over time. Initially, the 2002 Decree implementing Article 116 of the NRE identified some thirty disclosure categories.²¹⁸ These categories

²¹⁶ Loi 2010-788 du 12 juillet 2010 portant engagement national pour l'environnement [Law 2010-788 of July 12, 2010 on National Commitment to the Environment], JOURNAL OFFICIEL DE LA RÉPUBLIQUE FRANÇAISE [J.O.] [OFFICIAL GAZETTE OF FRANCE], July 12, 2010, p. 12905, art. 225.

²¹⁷ Décret 2012-557 du 24 avril 2012 relatif aux obligations de transparence des entreprises en matière sociale et environnementale [Decree 2012-557 of April 24, 2012 Regarding the Duties of Corporate Transparency in Social and Environmental], JOURNAL OFFICIEL DE LA RÉPUBLIQUE FRANÇAISE [J.O.] [OFFICIAL GAZETTE OF FRANCE], April 24, 2012, p. 7439 [hereinafter 2012 Decree]. Unofficial English translation available at http://www.rse-et-ped.info/IMG/pdf/12-04-26_Decret_225_French_Law_Reporting_English.pdf/.

²¹⁸ Décret 2002-221 du 20 février 2002 pris pour l'application de l'article L. 225-102-1 du code de commerce et modifiant le décret n° 67-236 du 23 mars 1967 sur les sociétés commerciales [Decree 2002-221 of February 20, 2002 Taken for the Application of Article L. 225-102-1 of the Commercial Code and Amending Decree 67-236 of March 23,

encompassed three broad areas of corporate activity, namely human resources and labor standards, community involvement, and environmental impact, management, and protection.²¹⁹ After Article 225 of the Grenelle II Law was enacted, the 2012 Decree listed forty disclosure categories, which are divided into three areas: social information (including employment, work organization, labor relations, health and safety training, equal opportunity and non-discrimination; for listed companies, promotion and enforcement of core labor standards of the International Labour Organization), environmental information (including environmental policy, pollution and waste management, sustainable usage of resources, climate change and protection of biodiversity), and social commitments in favor of sustainable development (including territorial, economic and social impact of the company's activity, relations with stakeholders such as social integration associations, educational institutions, environmental defense groups, consumer associations and the local population, use of outsourcing and suppliers).²²⁰

Even though the French NFR Law requires numerous categories of information to be disclosed, no specific reporting indicators are required and such disclosure categories do not correspond to any particular set of international CSR standards. There is no mandated form of reporting, although some guidance is given on the scope of the information to be provided. The requirement of third party verification was added by the 2012 Decree and now provides some assurance that company reports accurately portray their operations and are not being used merely to enhance their public image. As a result of a change made through the 2012 Decree, the French NFR Law adopts a “comply or explain approach,” meaning that a company may omit some of the required information if it is not considered relevant to its operations, but must present a rationale for such

1967 on Commercial Companies] JOURNAL OFFICIEL DE LA RÉPUBLIQUE FRANÇAISE [J.O.] [OFFICIAL GAZETTE OF FRANCE], Feb. 20, 2002, p. 3360.

²¹⁹ *Id.* at art. 1 (amending 1967 Decree to add Art. 148-2), art. 2 (amending 1967 Decree to add Art. 148-3).

²²⁰ 2012 Decree, *supra* note 217.

omissions, which then become subject to scrutiny by the third party auditor.²²¹

The French NFR Law does not impose sanctions for non-compliance with the disclosure mandate.²²² According to the French Office of the Ambassador at large for Corporate Social Responsibility, Article 116 was part of a long tradition of so-called “orientation laws” being regularly adopted in France to set national goals with the weight of parliamentary decisions behind them but without any government sanctions for non-compliance.²²³ It was incumbent on shareholders, who received such reports at the annual meeting, to apply pressure on company management to comply with the law if it failed to report.²²⁴ The 2012 Decree did not change this aspect of the French NFR Law to require any government sanctions for non-compliance.²²⁵

As a result of several of the key features of the French NFR Law, namely the “comply or explain” approach combined with the relative vagueness of the reporting standards and the lack of government sanctions for non-compliance, such law is considerably weaker than might appear at first glance. Rather than being a strong government mandate for enhanced disclosure, the French NFR Law leaves much to the discretion of business decision makers.

In spite of these weaknesses, some commentators believe that the French NFR Law has led to an increase in the quantity of non-financial reporting over time, although evidence of improvements in the quality of such reporting seems to be lacking. Initial studies showed a low rate of reporting under the French NFR Law and also revealed other problems relating to quality, such as wide variation in the form, content, length and

²²¹ *Id.*

²²² *See* Ministère des Affaires Etrangères – France: Office of the Ambassador At Large for Corporate Social Responsibility, *supra* note 213, at 1.

²²³ *Id.*

²²⁴ *Id.*

²²⁵ *Id.*

depth of reporting, use of only qualitative analysis and no quantitative measures by some companies, lack of documentation of sources in some cases, and no third party verification comparable to that used for financial reporting in most cases.²²⁶ Some private sector and academic commentators attributed such flaws to lack of experience in this type of reporting, as well as lack of reporting standards and ambiguities in the legal requirements.²²⁷ The lack of sanctions was considered by these commentators to be a positive feature because it encouraged experimentation and creativity in demonstrating a high level of reporting that could be emulated by other companies.²²⁸

The impact of the NRE's Article 116 mandate was assessed by auditing firms and by several associations involved with CSR reporting at the request of the French government and presented in a 2004 report ("2004 Report").²²⁹ In the 2004 Report, it was noted that there were approximately 700 companies to which the law applied, but not all were in compliance. The 2004 Report also pointed out the difficulty of formulating indicators for every area of sustainability, as well as the time-consuming and costly nature of such reporting. Such Report also attributed the low quality of reporting to a lack of consensus on key issues, including how comprehensive the indicators should be, whether such reports should be used for internal strategic and management purposes as well as to inform stakeholders, and the extent of company responsibility for foreign subsidiaries, suppliers, and subcontractors.²³⁰ Of particular concern in the

²²⁶ Egan et al, *supra* note 214, at 14.

²²⁷ *Id.*

²²⁸ Ministère des Affaires Etrangères – France: Office of the Ambassador At Large for Corporate Social Responsibility, *supra* note 213, at 2.

²²⁹ *Id.*; Entreprises pour l'Environnement (EpE), Entreprises et Collectivités: Partenaires pour l'Environnement (Orée), Observatoire sur la Responsabilité Sociétale des Entreprises (ORSE), *Abstract of the Mission Report Submitted to the Government: Critical Review of the Application of Article 116 of the NRE [New Economic Regulations] Law* (Apr. 2004), www.orse.org/fichier/2320.

²³⁰ Ministère des Affaires Etrangères – France: Office of the Ambassador At Large for Corporate Social Responsibility, *supra* note 213, at 2–3.

2004 Report was the need to connect such reporting to international frameworks, such as those developed by the United Nations, International Labour Organization, Organization of Economic Co-operation and Development, and the European Commission.²³¹ The 2004 Report concluded by emphasizing the need to allow non-financial reporting to evolve over time as companies became familiar with the requirements of the statute and tested them against international benchmarks.²³²

Notwithstanding such quality issues, the number of French companies who complied with the 2002 Decree requirements gradually increased over time. In a study by the French Ministry for Ecology and Development in 2007, it was reported that “81% of companies had at least made some effort” in non-financial reporting.²³³

In a 2013 document outlining its CSR strategy, the French government reported that its laws mandating non-financial reporting had led to “a marked change in quality” of such reporting.²³⁴ It also cited a 2011 study by the global accounting firm KPMG, which listed France in fourth place worldwide for such reporting by large companies, with an increase from 59% to 94% in a three year period.²³⁵ In addition, a 2015 study by KPMG found that the rate of CSR reporting in annual reports in France stood at 93%.²³⁶ Such 2015 report also observed a global increase in CSR reporting and attributed the increase to government regulation mandating such reporting.²³⁷

²³¹ *Id.* at 4.

²³² *Id.* at 5.

²³³ Ministère des Affaires Etrangères – France: Office of the Ambassador At Large for Corporate Social Responsibility, *supra* note 213, at 2.

²³⁴ République Française, *supra* note 209, at 11.

²³⁵ *Id.* at 11. See KPMG, International Survey of Corporate Responsibility Reporting 2011, at 10 (Figure 2).

²³⁶ KING & BARTELS, *supra* note 66, at 37.

²³⁷ *Id.* at 36.

The current version of the French NFR Law, namely Article 225-102-1 of the French Commercial Code, as amended, covers many but not all of the reporting requirements of the 2014 EU Directive.²³⁸ Accordingly, amendments to conform to such Directive are required, but are still pending at the time of writing of this article. Among other things, some disclosure categories must be added in the areas of human rights and anti-corruption and anti-bribery. In addition, national enforcement mechanisms must be put in place.

Interestingly, before France notified its national law implementing the 2014 EU Directive, the French legislature passed a law on February 21, 2017 going beyond the disclosure requirements of such Directive and requiring certain large companies to adopt strong due diligence measures sufficient to identify risks and to prevent violations of human rights and fundamental freedoms, health and safety, and damage to the environment that could result from the activities of each covered company, its subsidiaries, and companies it controls, as well as suppliers and subcontractors with which it has established commercial relationships.²³⁹ Such legislative development signals the continued willingness of French lawmakers to tackle important CSR issues through government action.

2. Denmark

Denmark is another Member State with a long-standing commitment to CSR. It was the first Member State to implement the 2014 EU Directive into its national law.²⁴⁰ It first introduced CSR reporting requirements for certain businesses in December 2008 through an Act amending the Danish Financial Statements Act (“FSA”) and entitled “Accounting

²³⁸ See 2012 Decree, *supra* note 217.

²³⁹ Loi n° 2017-399 du 27 mars 2017 relative au devoir de vigilance des sociétés mères et des entreprises donneuses d'ordre, available at <https://www.legifrance.gouv.fr/eli/loi/2017/3/27/2017-399/jo/texte>. The law survived a constitutional challenge and became effective on March 29, 2017.

²⁴⁰ Danish Financial Statements Act (“Årsregnskabsloven”), cf. Consolidated Act no. 647 of 15 June 2006, as amended by § 5 of Act no. 108 of 7 February 2007, § 63 of Act no. 468 of 17 June 2008 and Act no. 516 of 17 June 2008 [hereinafter 2008 Act].

for CSR in large businesses” (“2008 Act”).²⁴¹ The text of the 2008 Act and accompanying commentary were set forth in a 2008 document entitled “Proposal for an Act amending the Danish Financial Statements Act (Report on social responsibility for large businesses)” (“2008 Proposal”).²⁴² The 2008 Act became effective on January 1, 2009, and became applicable for financial years starting on January 1, 2009 and later.²⁴³

The reporting requirements were part of the Action Plan for Corporate Social Responsibility promulgated by the Danish government in May 2008 (“2008 CSR Action Plan”).²⁴⁴ Such Action Plan stated that the purpose of such reporting requirements was to enhance transparency so that stakeholders could influence the CSR policies of businesses and investors.²⁴⁵ Another stated reason for introducing the reporting requirements was to bolster the market shares of Danish businesses by demonstrating their commitment to sustainable growth.²⁴⁶ The 2008 Proposal for a law on CSR reporting that resulted in the 2008 Act noted these same two reasons for introducing CSR reporting requirements and also suggested such reporting would encourage businesses and investors to “contribute to solving social challenges” and in so doing, “create better business opportunities for themselves.”²⁴⁷

²⁴¹ *Id.* See Danish Business Authority, *Legislation*, CSRGOV, <http://csrgov.dk/legislation> (last visited Apr. 22, 2018).

²⁴² Danish Business Authority, *Proposal for an Act Amending the Danish Financial Statements Act (Report on Social Responsibility for Large Businesses)*, 1 CSRGOV (Oct. 8, 2008) [hereinafter 2008 Proposal], http://csrgov.dk/file/319999/proposal_report_on_social_resp_december_2008.pdf.

²⁴³ *Id.* at 3 (discussing the date the 2008 Act enters into force in Section 2).

²⁴⁴ The Danish Government, *Action Plan for Corporate Social Responsibility 1*, 21 CSRGOV (May 2008), http://csrgov.dk/file/318799/action_plan_CSR_september_2008.pdf.

²⁴⁵ *Id.*

²⁴⁶ *Id.*

²⁴⁷ 2008 Proposal, *supra* note 242, at 5.

The 2008 Act added new Section 99a to the FSA, which set forth the requirement that covered businesses include information in their annual reports on their CSR strategies.²⁴⁸ Covered businesses were large businesses in accounting class C under the FSA, and listed companies and state-owned companies in accounting class D under the FSA.²⁴⁹ The Danish Government calculated that approximately 1,100 companies would be covered by the 2008 Act.²⁵⁰ SMEs were not covered by the reporting requirement.²⁵¹

CSR was defined in the 2008 Act as “businesses voluntarily includ[ing] considerations for human rights, societal, environmental and climate conditions, as well as combating corruption in their business strategy and corporate activities.”²⁵² Although no specific reporting topics under these four broad subject matter areas were mandated in the text of the 2008 Act, the explanatory comments in the 2008 Proposal stated that Danish companies should base their policies on “an internationally recognised reference framework.”²⁵³ More specifically, the 2008 Proposal noted that the four subject matter areas included in the definition are based on the U.N. Global Compact categories, which in turn are elaborated through ten principles.²⁵⁴ While appearing to recommend the U.N. Global Compact principles as a basis for CSR reporting, the 2008 Proposal noted that such principles should not be viewed as “a checklist for completion by companies” and that companies should choose the areas that are relevant to their

²⁴⁸ *Id.* at 1 (discussing the insertion of Section 99a in Section 1, ¶ 1).

²⁴⁹ *Id.* at 6. Accounting class C covers both medium and large limited liability companies. Large businesses in accounting class C are businesses that exceed at least two of the following three size limits for medium-sized companies: total assets/liabilities of 143 million Danish Kroner (\approx 19.2 million Euros); net revenue of 286 million Danish Kroner (\approx 38.4 million Euros); an average of 250 full-time employees.

²⁵⁰ *Id.*

²⁵¹ *Id.* at 1, 6.

²⁵² 2008 Proposal, *supra* note 242, at 1 (adding the new Section 99a-(1)).

²⁵³ *Id.* at 4.

²⁵⁴ *Id.* at 9.

core businesses.²⁵⁵ In addition to the U.N. Global Compact, the 2008 Proposal suggested that the U.N. Principles for Responsible Investment, the OECD Guidelines for Multinational Enterprises, and the GRI frameworks were also useful sources for the content of CSR reporting.²⁵⁶

The annual report was required to contain information on the following three topics: (1) social responsibility policies of the business, including standards, guidelines or principles in use; (2) implementation of such policies, including systems or procedures in place; and (3) assessment of work on social responsibility initiatives, including expected future outcomes.²⁵⁷ No further or more specific guidance was given in the 2008 Act on the reporting format that should be used.²⁵⁸

While the 2008 Act stated that the required disclosure should be included in the management review section of the annual report, companies could instead choose to disclose in a supplementary statement to the annual report or on the business website.²⁵⁹ The location of such disclosure had to be stated and such disclosure had to be made available at the same time as the annual report.²⁶⁰ If a business was already reporting under the U.N. Global Compact or the U.N. Principles for Responsible Investment in the form of a Communication on Progress Report (“COP Report”), it was exempt from the reporting requirements of the 2008 Act, but instead was required to state in its annual report that it was taking advantage of the reporting exemption and to indicate where such COP Report was publicly available.²⁶¹

²⁵⁵ *Id.*

²⁵⁶ *Id.* at 10.

²⁵⁷ 2008 Act, *supra* note 240, § 99a-(2).

²⁵⁸ *See id.*

²⁵⁹ 2008 Act, *supra* note 240, § 99a-(3).

²⁶⁰ 2008 Proposal, *supra* note 242, at 8; 2008 Act, *supra* note 240, § 149a.

²⁶¹ 2008 Act, *supra* note 240, § 99a-(7).

The language of the 2008 Act made clear that adoption of CSR policies and reporting on CSR policies were separate matters.²⁶² Businesses with CSR policies in place were required to disclose in accordance with the requirements of the 2008 Act.²⁶³ Businesses were not required to adopt CSR policies in the first place, however.²⁶⁴ But if they did not, they had to disclose that fact in the annual report.²⁶⁵

The information disclosed pursuant to the 2008 Act requirements had to be checked by a company's auditor for consistency with financial statement disclosures (or consolidated financial statement disclosures) and was required to be covered by the auditor's opinion letter.²⁶⁶ However, there was no requirement for the auditor to verify that a company's business operations were consistent with its CSR policies.²⁶⁷

The Danish Government proposed further refinements to the 2008 CSR Action Plan in a document entitled "Responsible Growth: Action Plan for Corporate Social Responsibility 2012-2015 ("2012 CSR Action Plan").²⁶⁸ The 2012 CSR Action Plan set forth forty-two initiatives that were grouped into four topic areas, namely respecting international CSR principles, building partnerships among business, government and civil society, increasing transparency, and establishing good frameworks for responsible growth through public sector actions.²⁶⁹ Under the topic

²⁶² *Id.* § 99a(2)-(7).

²⁶³ *Id.*

²⁶⁴ 2008 Proposal, *supra* note 242, at 4.

²⁶⁵ 2008 Act, *supra* note 240, § 99a-(1).

²⁶⁶ 2008 Proposal, *supra* note 242, at 8.

²⁶⁷ Karin Buhmann, *The Danish Reporting Requirement as Reflexive Law: Employing CSR as a Modality to Promote Public Policy*, 1, 7-8, Univ. of Oslo Faculty of Law Legal Studies Research Paper Series No. 2011-36 (2011) (citing to Statutory Order No. 1305 16/12/2008, § 135; Statutory Order No 1043 05/11/2009, § 62; Statutory Order No. 1310 16/12/2008, § 132; Statutory Order No. 1307 16/12/2008, § 24).

²⁶⁸ The Danish Government, *Responsible Growth: Action Plan for Corporate Social Responsibility 2012-2015* 1, 4, 6-13 CSRGOV (Mar. 2012), http://csrgov.dk/file/318420/uk_responsible_growth_2012.pdf.

²⁶⁹ *Id.*

of transparency, the 2012 CSR Action Plan announced a change to the CSR reporting requirements for covered companies under the 2008 Act, namely a mandate to report on measures taken to respect human rights and reduce business impacts on climate.²⁷⁰

These reporting requirements were adopted by the Danish parliament on June 12, 2012, through an amendment to the FSA (“2012 Amendment”).²⁷¹ Such reporting was required even if these topics were not included in a covered company’s CSR policies. If a company did not have a policy on these topics, they were required to make a statement to that effect.²⁷² The purpose of the amendment was to encourage businesses to report on these two topics.²⁷³ However, the 2012 Amendment still did not require reporting on environmental, social and labor/employment-related matters or anti-corruption and anti-bribery matters.

After passage of the 2008 Act, the Danish Ministry of Business and Growth in collaboration with the Copenhagen Business School assessed the implementation of the non-financial reporting requirements on several occasions and issued reports.²⁷⁴ Such reports indicated that the

²⁷⁰ *Id.* at 11.

²⁷¹ Danish Financial Statements Act (“Årsregnskabsloven”), cf. Consolidated Act no. 647 of 15 June 2006, as amended by § 5 of Act no. 108 of 7 February 2007, § 63 of Act no. 468 of 17 June 2008 and Act no. 516 of 17 June 2008, and Act. no 117 of 21 May 2015.

²⁷² *Id.*

²⁷³ *Id.*

²⁷⁴ See e.g. Danish Commerce & Companies Agency, *Corporate Social Responsibility and Reporting in Denmark: Impact of the Legal Requirement for Reporting on CSR in the Danish Financial Statements Act* (Aug. 2010), https://samfundsansvar.dk/sites/default/files/corporate_social_responsibility_and_reporting_in_denmark_september_2010.pdf [hereinafter 2009 Report] (reporting on 2009 financial year); Danish Commerce & Companies Agency, *Corporate Social Responsibility and Reporting in Denmark: Impact of the Second Year Legal Requirements for Reporting on CSR in the Danish Financial Statements Act* (Nov. 2011), http://csrgov.dk/file/319199/corporate_social_responsibility_and_reporting_in_denmark_november_2011.pdf [hereinafter 2010 Report] (reporting on 2010 financial year); Danish Commerce & Companies Agency, *Corporate Social Responsibility and Reporting in Denmark: Impact of the Third Year Subject to the Legal Requirements for Reporting on CSR in the Danish Financial Statements Act* (Mar. 2013), https://samfundsansvar.dk/sites/default/files/csr_rapport_2013_eng.pdf (reporting on 2011 financial year); Danish Com-

reporting requirements had had a positive effect on businesses' work on CSR.²⁷⁵ According to such reports, over time, the number of covered companies reporting as required under the FSA had increased.²⁷⁶ However, it was also observed that further improvement was needed. For example, absence of reporting by some companies, lack of consistency in reporting, and failure of auditors to note deficiencies in company reporting, were mentioned.²⁷⁷ Lack of consistency in reporting referred to failure to disclose in all three required categories across all CSR policy topics.²⁷⁸ Auditors sometimes failed to mention the observed lack of consistency in their reports and they also failed to note errors and omissions in some cases.²⁷⁹ Most companies used qualitative reporting and few made use of indicators like those developed by the GRI.²⁸⁰

On the other hand, the government reports stated that there were also positive developments such as the increased familiarity by companies with the statutory requirements leading to less time invested in reporting, gradual integration of CSR in business strategies, and development of concrete steps to improve CSR initiatives and CSR reporting.²⁸¹ The government reports also noted that it had become increasingly common for companies to use international CSR principles as the basis for their reporting, especially the U.N. Global Compact.²⁸² The government believed that the

merce & Companies Agency, *Executive Summary Financial Year 2013*, at 1, http://csr.gov.dk/file/536161/executive_summary_report_financial_year_2013.pdf [hereinafter 2013 Report] (reporting on the implementation of the 2008 Act about the financial year 2013).

²⁷⁵ 2009 Report, *supra* note 274, at 1.

²⁷⁶ 2010 Report, *supra* note 274, at 2.

²⁷⁷ *Id.* at 5–6.

²⁷⁸ *Id.* at 3.

²⁷⁹ *Id.* at 6.

²⁸⁰ 2009 Report, *supra* note 274, at 12. Only 38% of companies used indicators and only 9% used the GRI indicators. *Id.*

²⁸¹ 2010 Report, *supra* note 274, at 6.

²⁸² *Id.* at 15. Some 34% of covered companies used international CSR standards for reporting in 2010. *Id.*

statutory reporting requirements were the reason that an increasing number of Danish companies, some 20% of covered companies, had subscribed to the U.N. Global Compact.²⁸³

In the most recent such report covering the financial year 2013, the Danish Government assessed compliance by the estimated 1,100 covered companies with the statutory requirements on CSR reporting. It was reported that 96% of such companies disclosed whether they had a CSR policy, and of these, 77% disclosed that they did.²⁸⁴ Of those companies with CSR policies, 97% disclosed the contents of such policy, 90% reported on their implementation of such policy, and 83% assessed the impacts of their work on CSR.²⁸⁵ Regarding the requirements to account for policies relating to human rights and climate impacts, 66% and 72% of companies, respectively, complied.²⁸⁶ The topics most frequently included were, in descending order of frequency, environmental matters, social conditions, climate impacts, anti-corruption, and human rights.²⁸⁷ The majority of covered companies placed the required CSR information in the management review section of the annual report, with the rest of the companies using a supplementary report in most cases and a smaller number posting the disclosure on the company's website.²⁸⁸

Pursuant to the mandate of the 2014 EU Directive to implement non-financial reporting requirements into national laws, the FSA was amended on May 21, 2015 ("2015 Act").²⁸⁹ The 2015 Act contained new

²⁸³ *Id.*

²⁸⁴ 2013 Report, *supra* note 274, at 1.

²⁸⁵ *Id.*

²⁸⁶ *Id.*

²⁸⁷ *Id.*

²⁸⁸ *Id.* at 2.

²⁸⁹ See Danish Business Authority, *Implementation in Denmark of EU Directive 2014/95/EU on the Disclosure of Non-financial Information*, CSRGOV 1 (May 2015), <http://csr-gov.dk/file/557863/implementation-of-eu-directive.pdf> [hereinafter 2015 Act].

requirements for CSR reporting. This was the first implementation of the 2014 EU Directive by any Member State.²⁹⁰

The 2015 Act goes beyond the requirements of the 2014 EU Directive by widening its applicability to include all covered companies subject to the CSR reporting requirements under the FSA. The 2014 EU Directive required Member States to enact legislation covering, at a minimum, companies that fall into the category of PIEs with at least 500 employees.²⁹¹ Prior to the 2015 Act, the CSR reporting requirements of the FSA applied to large businesses in accounting class C and to all entities in accounting class D.²⁹² While the FSA does not use the term PIEs, under such Act, businesses in accounting class D, i.e. listed companies and state-owned companies, are deemed to be of public interest. There are approximately 50 such companies with at least 500 employees out of the approximately 1,100 covered companies subject to the CSR reporting requirements of the FSA.²⁹³ For those companies, the 2015 Act requirements will take effect for financial years starting on or after January 1, 2016. For the other approximately 1,050 covered companies, the 2015 Act requirements will be applicable for financial years commencing on or after January 1, 2018.²⁹⁴

At the time the 2015 Act was passed, the Danish government stated that the 2014 EU Directive was based on the same principles as the CSR reporting requirements in the FSA. Both provided for “fundamental flexibility” for business, meaning that covered companies voluntarily decided whether to adopt a CSR policy and merely had to “be open about the choices they make.”²⁹⁵ Notwithstanding such common ground, there

²⁹⁰ *Denmark Transposes EU NFR Directive*, GRI, (July 1, 2015), <https://www.globalreporting.org/information/news-and-press-center/Pages/DENMARK-TRANSPPOSES-EU-NFR-DIRECTIVE.aspx>.

²⁹¹ 2014 EU Directive, *supra* note 12.

²⁹² 2008 Proposal, *supra* note 242, at 6.

²⁹³ 2015 Act, *supra* note 289, at 4.

²⁹⁴ *Id.* at 1.

²⁹⁵ *Id.* at 4.

were additional requirements contained in the 2014 EU Directive that necessitated changes to the FSA and that the 2015 Act incorporated in amended Section 99a. The 2014 EU Directive required companies to report, at a minimum, “environmental policies, including measures to reduce the climate impacts of the undertaking’s activities as well as social conditions and employee conditions, respect for human rights, and measures to fight bribery and corruption.”²⁹⁶ Businesses must comply with this requirement or, if they do not have such policies, explain the reasons, which requirement has been labelled “comply or explain”.²⁹⁷ Prior to the 2015 Act, covered companies under the FSA were only required to report on human rights and climate impact policies and were allowed to report on other categories on a voluntary basis. If they had no policies in the two required categories or no CSR policies at all, they merely had to make a statement to that effect. Due to the need to comply with the minimum requirements of the 2014 EU Directive, the 2015 Act requires covered companies to describe their CSR policies in at least the areas listed in the 2014 EU Directive, including any standards, guidelines or CSR principles used.²⁹⁸ For each policy area, a covered company must state whether it has a policy for such area and the nature of the policy.²⁹⁹ Following the “comply or explain” approach of the 2014 EU Directive, if a covered company does not have a policy in one or more of the enumerated areas, it must then disclose this fact, along with the reasons for such omission, in the case of each omitted policy area.³⁰⁰

Although the 2015 Act only specifies the minimum topic areas that are the subject of CSR policy disclosure, and does not recommend or require a specific reporting standard, the accompanying commentary provides greater detail on the content of such required disclosure than was

²⁹⁶ *Id.* at 2 (citing 2014 EU Directive, *supra* note 12).

²⁹⁷ *Id.* at 4; *see* 2014 EU Directive, *supra* note 12, at art. 1, ¶ 1 (referring to Article 19a-(1)).

²⁹⁸ 2015 Act, *supra* note 289, at 2 (discussing the addition of Section 99a-(2), subsection (2)).

²⁹⁹ *Id.*

³⁰⁰ *Id.* at 4, 10 (discussing the addition of Section 99a-(3)).

previously available to Danish companies.³⁰¹ While such guidance is helpful, the 2015 Act still fails to mandate a uniform reporting standard and it does not require the use of non-financial key reporting indicators. Rather than developing a Danish reporting standard or adopting one of the many available international standards as the basis for CSR reporting, the amended FSA does not go beyond the minimum requirements of the 2014 EU Directive in this regard.

Other changes to the FSA necessitated by the 2014 EU Directive and implemented through the 2015 Act include requirements for covered companies to disclose their business models, due diligence processes implemented, principal risks related to business activities including those with a special risk of negative impacts in the enumerated CSR policy areas and related risk management strategies, and use of non-financial key performance indicators, if any.³⁰² These new requirements build upon and expand the 2008 Act language on reporting on the existence, implementation, and assessment of CSR policies.³⁰³ However, there is no uniform reporting format mandated.

Other requirements of the 2008 Act touching on location of the CSR statement in the management review section or alternatives for satisfying the disclosure requirement, reporting requirements for subsidiaries and corporate groups, and audit requirements remain fundamentally unchanged.³⁰⁴ The 2015 Act grants authority to the Danish Business Authority to promulgate rules on alternative means of disclosing required information if not contained in the management review section and on the terms of CSR reporting according to international guidelines and principles.³⁰⁵

³⁰¹ *See id.*

³⁰² 2015 Act, *supra* note 289, at 2 (discussing the addition of Section 99a-(2), subsections (3)–(5)).

³⁰³ 2008 Proposal, *supra* note 242, at 9.

³⁰⁴ 2015 Act, *supra* note 289, at 11–14.

³⁰⁵ *Id.* at 3 (discussing the addition of Section 99a-(8) and (9)).

Since the 2015 Act only became effective for PIEs with more than 500 employees for financial years starting in January 2016 and after, it is too soon to assess the impact of the new CSR reporting requirements on the basis of actual reporting trends, as was done in prior years by the Danish government. However, some commentators have already weighed in, predicting that the more specific requirements mandated by the 2014 EU Directive and implemented in the 2015 Act will increase the quantity but not the quality of CSR reporting.³⁰⁶ This is attributable to the failure to set forth detailed rules and standards for the collection and processing of non-financial information.³⁰⁷

IV. CRITIQUE OF THE NEW EUROPEAN UNION APPROACH TO NON-FINANCIAL REPORTING

At the time of its adoption, the 2014 EU Directive was lauded by then European Commissioner for Internal Market and Services Michel Barnier as an important step forward in “modernising the disclosure of relevant and useful non-financial information”³⁰⁸ According to Commissioner Barnier, such transparency leads to companies taking a “longer term perspective in their decision-making . . . [leading to] lower financing costs, attract[ing] and retain[ing] talented employees, and ultimately [becoming] more successful,” consequences that are “important for Europe’s competitiveness and the creation of more jobs.”³⁰⁹

Although the Directive represents a significant achievement for the EU because it promotes CSR reporting among a large group of countries with significant business interests, namely the 28 Member States, there are a number of troubling issues that can be raised about the Directive and unanswered questions concerning its effectiveness still remain.

³⁰⁶ Daniel Gergely Szabo & Karsten Engsig Sorensen, *New EU Directive on the Disclosure of Non-financial Information (CSR)*, 12 EUR. CO. AND FIN. L. REV. 307, 331–332 (2015).

³⁰⁷ *Id.*

³⁰⁸ European Commission Statement, *Improving Corporate Governance: Europe’s Largest Companies Will Have to be More Transparent About how They Operate*, EUROPEAN COMMISSION PRESS RELEASE DATABASE (Apr. 15, 2014), http://europa.eu/rapid/press-release_STATEMENT-14-124_en.htm [hereinafter 2014 EC Statement].

³⁰⁹ *Id.*

This Section IV will critique the 2014 EU Directive and the trend it represents for non-financial reporting. It will also speculate about the possibility that the Directive as adopted will not achieve its stated policy goal of improving non-financial reporting in Europe.

A. Critique of the 2014 EU Directive

There are several weaknesses of the 2014 EU Directive that will be addressed in this Section IV.A. These include its limited coverage of enterprises, lack of uniform reporting standards, too much flexibility for covered businesses regarding content and location of disclosure, lack of strong verification requirements, and lack of strong penalties or other remedies for disclosure violations.

1. Limited Coverage of Enterprises

First, the 2014 EU Directive is applicable only to large PIEs and also does not cover SMEs. These features limit the impact that the 2014 EU Directive will have. As the 2014 EU Directive was originally proposed, it was applicable to companies with an average number of employees exceeding 500 during the financial year and with a balance sheet total of at least EUR 20 million or a net turnover of EUR 40 million.³¹⁰ The EU estimated that such proposed Directive would apply to 18,000 entities.³¹¹ However, as adopted, the 2014 EU Directive was applicable only to PIEs with an average number of employees exceeding 500 during the financial year.³¹² As a result, the number of entities that will be covered is estimated to be only 6,000, two-thirds less than the original number of entities that would have been covered under the proposed Directive.³¹³ This was a curious policy choice in view of the fact that the European Commission had noted that the purpose of the 2014 EU Directive was to

³¹⁰ See 2013 EU Impact Assessment, *supra* note 183, at 5, 11.

³¹¹ *Id.*

³¹² 2014 EU Directive, *supra* note 12, at 4 (concerning new Article 19a(1)).

³¹³ Press Release, *Newly Approved European Legislation on Non-financial Information Disclosure Sends Strong Signals to Companies, but Falls Short of Responsible Investors' Expectations*, EUROSIIF (Apr. 15, 2014), http://www.eurosif.org/wp-content/uploads/2014/05/press-release_non-financial-information-disclosure-legislation.pdf.

address the inadequate transparency of non-financial information, both in quantity and quality.³¹⁴ The European Commission had noted that only an estimated 2,500 out of a total of 42,000 EU large companies formally disclosed non-financial information on an annual basis.³¹⁵ It also noted quality issues in information that was disclosed, finding that such information was “often lacking in materiality, or not sufficiently balanced, accurate and timely,” as well as showing gaps in reporting on “policies and risk-management, as well as on specific topical areas (human rights, corruption).”³¹⁶

In addition, the 2014 EU Directive does not cover SMEs. In the 2011 CSR Strategy, the European Commission noted that its new definition of CSR, namely “the responsibility of enterprises for their impacts on society,” required that enterprises integrate CSR into their business operations and core strategies.³¹⁷ However, the European Commission also noted that for SMEs, such CSR process was likely “to remain informal and intuitive.”³¹⁸ This language signaled that SMEs would be treated differently than large enterprises in respect of their CSR obligations. The 2011 CSR Strategy went on to suggest that the European Commission would support capacity building for SMEs.³¹⁹

In both the 2014 EU Directive and the 2013 EU Proposal, the European Commission stated that the overall regulatory burden for business at both the European and national levels should be reduced, especially for SMEs.³²⁰ Both documents stated that the non-financial disclo-

³¹⁴ 2013 EU Impact Assessment, *supra* note 183, at 10.

³¹⁵ *Id.* at 10.

³¹⁶ *Id.* at 11, 28.

³¹⁷ 2011 CSR Strategy, *supra* note 167, at 3.

³¹⁸ *Id.*

³¹⁹ *Id.*

³²⁰ 2014 EU Directive, *supra* note 12, at preamble, recital 13; 2013 EU Proposal, *supra* note 180, ¶ 10.

sure requirements should be made applicable only to certain large enterprises and that SMEs should be exempted from such requirements.³²¹ The basis for this policy decision was further explained in the 2013 EU Impact Assessment, in which it appears that in the public consultations held in connection with the 2013 EU Proposal, the interests of the users of non-financial information emerged as being at odds with the reporting preferences of the providers of such investors. While investors and non-governmental organizations argued that the costs of reporting would be outweighed by the benefits to civil society due to increased transparency and the ability to make investment decisions based on a long-term perspective, the majority of businesses argued that stricter disclosure requirements could be overly burdensome, in particular for SMEs, and impact competitiveness.³²²

Political scientist Daniel Kinderman, who has studied the political dynamics and interest group activities associated with CSR initiatives in Europe, has noted that the reason for the exclusion of SMEs was due to German opposition, particularly from the business sector, which includes many SMEs.³²³ As he has pointed out, the original proposal for the Directive was intended to cover a larger group of enterprises, but it was considerably watered down in a number of respects, including the entities that would be covered, due to opposition from the business community, especially in Germany.³²⁴ Based on Kinderman's account of the negotiations over the 2014 EU Directive, three countries exerted the most influence, namely France, the United Kingdom, and Germany, with France being the strongest supporter and attempting to strengthen the original proposal, Germany rejecting the entire proposal, and the United Kingdom proposing amendments to water down the proposal in some respects even

³²¹ 2014 EU Directive, *supra* note 12, at ¶ 13-14; 2013 EU Proposal, *supra* note 180, at ¶ 11.

³²² 2013 EU Impact Assessment, *supra* note 183, at 45.

³²³ Kinderman, *supra* note 198.

³²⁴ *Id.*

though it has been supportive of non-financial reporting in the past.³²⁵ When the European Commission announced its 2011 CSR Strategy, the largest and most powerful organizations of businesses in Germany opposed the idea of regulation, stating that the European Commission was encroaching on corporate discretion and that non-financial reporting should remain voluntary.³²⁶ In particular, this German coalition of businesses stated that “[t]he bureaucratic burden—especially for small and medium-sized companies—would be considerable and greatly outweigh any benefits.”³²⁷ The German federal government supported the stance of German businesses, stating in a government position paper that it was opposed to “new statutory duties to disclose social and environmental information [since] [t]hese would amount to a departure from the voluntary principle and would entail considerable bureaucracy, particularly for small and medium-sized enterprises in Germany.”³²⁸

2. Lack of Uniform Reporting Standards

Second, the 2014 EU Directive does not adopt uniform reporting standards as to content or format and does not require the use of key performance indicators, such as those contained in the GRI frameworks. The European Commission was directed to prepare guidelines to facilitate disclosure, taking into account international best practices. As discussed in Section III.A above, the European Commission did in fact issue the 2017 NFR Guidelines. However, such Guidelines do not add much detail to what is set forth in the 2014 EU Directive regarding the content or format of reporting. The Guidelines do provide some examples of material information that companies could consider disclosing, along with examples of related key performance indicators that they might also include. However, the 2017 NFR Guidelines do not suggest any particular reporting framework for use by the Member States. There are numerous such

³²⁵ *Id.*

³²⁶ *Id.*

³²⁷ *Id.*

³²⁸ *Id.*

reporting frameworks to choose from, as discussed in Section III.A above. Instead, the 2017 NFR Guidelines merely repeat language from the 2014 EU Directive that states “[a] company may rely on high quality, broadly recognized national, EU-based or international frameworks when preparing its non-financial statement” and states further that companies should disclose which frameworks they used for specific disclosures to enhance clarity and comparability.³²⁹ This language adds no clarification regarding the requirements of the 2014 EU Directives and therefore provides no useful guidance to Member States. Moreover, it must be remembered that such Guidelines are not binding on the Member States, further weakening their usefulness.

The lack of a recommended reporting standard is at odds with current practice among companies, many of whom have adopted the GRI frameworks to use for their non-financial reporting. A better approach than the flexible approach of the 2014 EU Directive would be to adopt a framework that has become the gold standard in sustainability reporting, namely the GRI frameworks. As discussed in Section II above, the 2015 KPMG Report states that three-quarters of Global Fortune 250 companies use the GRI frameworks.³³⁰ In addition, the GRI has formed alliances with institutional partners such as the U.N. Global Compact, and in that way, actively promotes convergence around its key indicators. Finally, the GRI frameworks have been adopted in some national legislation.

The GRI approach has its critics. Among them is law professor Galit Sarfaty, who has criticized the GRI frameworks for promoting a check the box mentality.³³¹ It has been described as “accountant driven,” suggesting that there is no lawyerly input on disclosure areas where legal expertise is helpful, such as in the area of human rights norms and compliance. It lacks a focus on impacts and it lacks uniform guidelines on third party assurances. It divides indicators into core indicators and op-

³²⁹ 2017 NFR Guidelines, *supra* note 122, § 5.

³³⁰ KING & BARTELS, *supra* note 66, at 42.

³³¹ Galit A. Sarfaty, *Regulating Through Numbers: A Case Study of Corporate Sustainability Reporting*, 53 VA. J. INT'L L. 575, 606 (2013).

tional indicators, although some of the optional indicators may be important to certain stakeholders. It fosters a culture of a reporting treadmill in which the focus is on extensive data gathering, leaving few resources that can be devoted to organizational change. The GRI rankings focus on the level of disclosure rather than the quality and accuracy of sustainability performance.

Notwithstanding these shortcomings, the GRI frameworks have the benefit of having gained broad acceptance in the business community and are widely recognized around the world. As of yet, no second-best alternative has emerged to challenge the preeminence of the GRI frameworks, at least among large companies such as those in Global Fortune 250.

The 2014 EU Directive adopts a minimum harmonization approach, meaning that Member States are required to meet only the minimum requirements set forth in the Directive, although they are free to adopt higher standards if they choose. The European Commission considered a wide range of alternative approaches to non-financial reporting requirements apart from the minimum harmonization approach that was eventually incorporated in the Directive. In the 2013 EU Impact Assessment, the European Commission outlined these policy options and also assessed such policy options against the criteria of effectiveness in meeting the objectives of the Directive, including compliance costs, competitiveness, and coherence with other EU legislation.³³² Full harmonization through the introduction of detailed reporting requirements in accord with an internationally accepted standard and full harmonization through the adoption of a new mandatory EU standard developed specifically for this purpose were also considered.³³³ The 2013 EU Impact Assessment concluded that there would be benefits from such full harmonization approaches, noting that full harmonization through mandatory EU standards would “increase significantly the quantity and quality of disclosed information” that would “generate economic benefits resulting from better

³³² 2013 EU Impact Assessment, *supra* note 183, at 29–30.

³³³ *Id.* at 25–30.

management and allocation of capital and an overall positive environmental and social impact.”³³⁴ Both of these alternatives were rejected on the grounds that such requirements would impose administrative burdens and would not be cost-effective. In the case of the mandatory EU standards approach, the European Commission also was concerned about “the completion of a long and uncertain process of development and implementation of such standards, including thorough consultation with stakeholders.”³³⁵ A final concern was with critics who thought the full harmonization approaches would lead to “tick the box” compliance that would have “only limited impact on real companies’ behavior.”³³⁶

The minimum harmonization approach may not prove optimal for companies that operate across national borders, which is the case for many of the large PIEs covered by the 2014 EU Directive. This is because such enterprises will incur additional costs if they are required to comply with varying disclosure requirements in different Member States. Since Member States are only required to meet the minimum standards set forth in the Directive and not a set of EU prescribed standards or the standards imposed by a designated international framework, disclosure requirements may well vary among Member States. In addition, the minimum harmonization approach may not prove optimal for investors who seek comparability across companies. Shares of listed companies covered by the 2014 EU Directive are often traded across national borders, creating a need on the part of investors for comparability of information. The minimum harmonization approach does not facilitate comparison of non-financial reporting between listed companies in different Member States.³³⁷

³³⁴ *Id.* at 29.

³³⁵ *Id.*

³³⁶ *Id.*

³³⁷ Daniel Gergely Szabo & Karsten Engsig Sorensen, *New EU Directive on the disclosure of non-financial information (CSR)*, NORDIC AND EUROPEAN COMPANY LAW, LSN Research Paper Series, No. 15-01 (2015), at 8 (citing European Commission Staff Working Document, Impact Assessment, 164.2013, at 24–31).

The extremely flexible approach taken to the content and format of such reporting seems at odds with the statements that have been made over the years in EU policy statements and in the 2014 EU Directive itself regarding the need for uniformity and consistency in non-financial reporting. For example, the 2014 EU Directive listed one of its policy goals as “the consistency and comparability of non-financial information . . . throughout the Union” and “coordination of national provisions concerning the disclosure of non-financial information in respect of certain large undertakings . . . [which is] necessary . . . because most of those undertakings operate in more than one Member State.”³³⁸ In the 2001 Green Paper in which the European Commission started to develop a CSR policy for the EU, the Commission noted that some of the problems associated with CSR reporting included lack of consistency in content, reporting format and use of reliability and audit standards, as well as the proliferation of reporting frameworks and the lack of coherence among such standards.³³⁹ The Commission also noted the emergence of the GRI Guidelines as evidence of best practices on environmental reporting.³⁴⁰ These statements of EU policy goals are evidence that the European Commission is well aware of the problems associated with consistency and comparability among EU companies engaged in non-financial reporting. Yet it chose to adopt the 2014 EU Directive, which failed to fully address many of the issues noted in its policy statements.

Some of the weaknesses of the 2014 EU Directive may be attributable to concerns about imposing costs associated with such reporting on businesses. In fact, in the 2013 EU Impact Assessment that preceded adoption of the 2014, EU Directive, the European Commission calculated the costs of the new disclosure requirements relating to drafting, publication, and specific staff training or data collection, both on a per company and total costs basis.³⁴¹

³³⁸ 2014 EU Directive, *supra* note 12, at preamble, recitals 4, 6.

³³⁹ 2001 Green Paper, *supra* note 130, at 16, 17.

³⁴⁰ *Id.* at 17.

³⁴¹ 2013 EU Impact Assessment, *supra* note 183, at 39.

This lack of uniform reporting standards in the 2014 EU Directive may limit the usefulness of CSR reporting for investors seeking to compare businesses from different Member States and may create difficulties for companies operating across national borders. The lack of a requirement for use of key performance indicators also calls into question whether there will be any improvement in the quality of CSR reporting as a result of the Directive.

3. Too Much Flexibility Given to Covered Businesses

Third, although the 2014 EU Directive has been described as “mandating” CSR reporting, it provides a great deal of “flexibility” to businesses on the nature of their CSR reporting, including its content and place of publication, and even on the question of whether businesses need to report at all. Examples of such flexibility include the “comply or explain” approach to the content of non-financial reporting, namely the option of businesses to omit reporting on issues for which they have failed to adopt policies, as long as they provide a reasoned explanation for why such policies are not in place.³⁴² This provision seemingly undercuts incentives reporting companies would otherwise have to improve their performance on CSR topics since they are not held accountable for failing to adopt policies in the first place. Another example is the option of business to deviate from the requirement of including non-financial reporting in their annual reports, which requirement would make such information readily accessible to investors and other stakeholders along with financial and other relevant disclosure mandated in such reports. Instead, companies issuing standalone reports may substitute such reporting for the required annual report statement and may provide such information on their websites. This may prove convenient for management but may make the information more difficult to find and access for investors and other stakeholders.

The European Commission has described the regulatory approach of the 2014 EU Directive as “smart regulation” or a “smart mix approach”

³⁴² 2014 EU Directive, *supra* note 12, at art. 1, ¶ 1 (discussing “Non-financial statement” in new Article 19a, ¶ 1).

involving a mixture of policy approaches combining government regulation that allows significant choices about disclosure to be made on a voluntary basis by businesses.³⁴³ As such, the “smart mix approach” represents an intermediate position that bridges the gap between voluntary disclosure and mandatory reporting requirements.

The “smart mix approach” of the 2014 EU Directive might be viewed as an example of reflexive regulation, an emerging concept that some commentators have advocated as a mechanism to govern corporate behavior. Reflexive regulation stands in contrast to substantive government regulation of business, which commentators have criticized for its lack of effectiveness in producing socially responsible behavior.³⁴⁴ It has been described as “a regulatory system that recognizes the limited ability of the law in a complex society to direct social change in an effective manner” through a process that “aims to guide behavior and promote self-regulation.”³⁴⁵ Such regulation is deemed reflexive because “it encourages corporations to constantly re-examine their practices and reform those practices based on the most current information.”³⁴⁶ Business school professor David Hess has suggested that CSR could be promoted through a reflexive law approach to what he termed “social reporting,” which appears to be synonymous with non-financial reporting as defined in this article.³⁴⁷ He believes that social reporting will lead to improved corporate decision-making that is responsive to expectations of stakeholders, as such expectations change over time.³⁴⁸

³⁴³ See 2011 CSR Strategy, *supra* note 167, at 7.

³⁴⁴ David Hess, *Social Reporting: A Reflexive Law Approach to Corporate Social Responsiveness*, 25 J. CORP. L. 1, 58 (1999).

³⁴⁵ *Id.* at 42–43 (quoting Eric W. Orts, *A Reflexive Model of Environmental Regulation*, 5 BUS. ETHICS Q. 779, 780 (1995)).

³⁴⁶ *Id.* at 43 (quoting Eric W. Orts, *A Reflexive Model of Environmental Regulation*, 5 BUS. ETHICS Q. 779, 780 (1995)).

³⁴⁷ *Id.* at 62.

³⁴⁸ *Id.* at 63.

In principle, building flexibility into government instruments on non-financial reporting through use of such a reflexive regulation approach may lead to greater CSR. However, in the case of the 2014 EU Directive, such flexibility may be viewed as weakening the mandate for enhanced reporting. It may be the case that building flexibility into the Directive was a necessary compromise given the strong opposition by business to government regulation of non-financial reporting, as reported by commentators like Kinderman, among others.³⁴⁹ The “flexibility” to deviate from the requirements of the 2014 EU Directive may be attractive to businesses seeking to design their own CSR programs without interference from government regulators. However, such flexibility may undercut incentives to improve existing non-financial reporting and CSR policies of businesses. This approach calls into question whether the 2014 EU Directive will have its intended impact of increasing transparency and its suggested attendant benefits.³⁵⁰

4. Lack of Strong Verification Requirements

Fourth, the 2014 EU Directive does not require Member States to provide for verification of the truthfulness of the non-financial information disclosed by companies, although the statutory auditor will be required by Member States to check whether the non-financial statement has been provided.³⁵¹ The Directive states that Member States “may require that the information in the non-financial statement . . . be verified by an independent assurance services provider,” but there is no firm requirement that such verification be provided.³⁵² The lack of a requirement for third party assurances that what is being reported by companies accurately reflects their policies can be viewed as weakening the non-financial reporting requirements and may lead stakeholders to question the veracity

³⁴⁹ Kinderman, *supra* note 198.

³⁵⁰ 2014 EC Statement, *supra* note 308, at 1.

³⁵¹ 2014 EU Directive, *supra* note 12, at art. 1, ¶ 1 (discussing “Non-financial statement” in new Article 19a, ¶ 5).

³⁵² *Id.* at art. 1, ¶ 1 (discussing “Non-financial statement” in new Article 19a, ¶ 6).

of the information provided by companies, thereby undermining its usefulness. It also limits the incentives companies may have to provide accurate and complete information.

5. Lack of Strong Penalties or Other Remedies for Disclosure Violations

Fifth, there are no consequences or penalties for non-disclosure spelled out in the Directive. This is left to the Member States to decide with the Directive stating in the preamble only that “Member States should ensure that effective national procedures are in place to enforce compliance with the obligations laid down by this Directive.”³⁵³ This provision allows Member States to put in place their own compliance mechanisms and remedies, but not to conform to any particular standard. This provision potentially weakens the mandate of the 2014 EU Directive by failing to require strong enforcement mechanisms to address non-compliance.

B. Likelihood of Success of the 2014 EU Directive

The preceding Section IV.A of this paper set forth several reasons that the 2014 EU Directive may be viewed as a weak mandate for non-financial reporting by companies in EU Member States. The consequence of the flaws in the 2014 EU Directive is that such Directive may be ineffective in achieving its policy goals of increased transparency by companies and the supposed attendant benefits that motivated the European Commission to adopt the Directive in the first place.

It is not possible currently to assess the effectiveness of the 2014 EU Directive in achieving its stated policy goals. For one thing, not all Member States have transposed the Directive into their national laws and

³⁵³ *Id.* at preamble, recital 10.

for those that have, the European Commission has noted that some Member States' laws fail to conform to the Directive.³⁵⁴ Even more importantly, the requirements of the Directive are applicable only to fiscal years beginning on January 1, 2017, or during calendar year 2017.³⁵⁵ Many companies have not yet reported under the new requirements, so it is impossible to determine at this point whether the concerns expressed above about flaws in the 2014 EU Directive will prove valid or not. Such an assessment cannot be made until more time has passed, the EU Member States take further action to implement the Directive into their national laws, and companies adopt new reporting practices for CSR information. Empirical studies will be needed at such future date to determine how such new reporting practices are working, including whether the Directive is fostering a higher quantity and quality of non-financial reporting and whether such information is fulfilling the informational needs of stakeholders.

In the meantime, however, it is possible to speculate about the likelihood that the 2014 EU Directive will foster better CSR reporting practices, based on studies that appear in the accounting literature. There is a body of academic literature in the field of sustainability accounting that questions whether government regulation mandating non-financial disclosure alone results in better levels of disclosure. The literature consists of empirical studies of the impact of mandatory CSR reporting laws that were in place prior to adoption of the 2014 EU Directive. Several of such studies have concluded that mandating CSR reporting has had only limited success in increasing the number of companies reporting or the quality of such reporting. This body of literature is relevant to the question of whether the 2014 EU Directive will result in improved CSR reporting.

For example, Luque-Vilchez and Larringa studied the impact of Spain's 2011 Sustainable Economy Law ("2011 SEL") and concluded that it was a failure, having no impact in terms of the number of companies

³⁵⁴ See European Commission, Non-financial reporting directive – transposition status, *supra* note 204.

³⁵⁵ 2014 EU Directive, *supra* note 12, at art. 4, ¶ 1.

that reported and a slight impact in terms of improved quality of reporting.³⁵⁶ From their empirical work, the authors concluded that disclosure regulation by itself may be insufficient to improve CSR reporting. The authors identified several reasons for the limited impact of the mandatory reporting law. First, there was no consensus on the meaning of CSR that emerged after stakeholder consultations convened by the Spanish government prior to enactment of the law.³⁵⁷ Instead, the authors contend that there was conflict between members of the corporate and civil society camps.³⁵⁸ Business argued for voluntary reporting, while civil society favored mandatory reporting.³⁵⁹ This lack of shared expectations made it difficult for a consensus to emerge.³⁶⁰ Second, the practices mandated by the 2011 SEL did not correspond to existing reporting norms.³⁶¹ Prior to the 2011 SEL, large companies issued sustainability reports using the GRI frameworks as a standard and they continued to do so even after enactment of the 2011 SEL.³⁶² Finally, there was no enforcement mechanism put in place by the 2011 SEL, leading to a lack of clarity on what constituted compliance with the law. According to the authors, this could have been clarified by setting forth guidelines for reporting and a process for submitting CSR reports to the relevant regulator, namely the State Council of Corporate Social Responsibility.³⁶³

These conclusions about the lack of effectiveness of government mandates are consistent with those reported in other published studies.

³⁵⁶ Mercedes Luque-Vilchez & Carlos Larrinaga, *Reporting Models Do Not Translate Well: Failing to Regulate CSR Reporting in Spain*, SOC. & ENVTL. ACCOUNTABILITY J., 36:1, 56–75 (2016).

³⁵⁷ *Id.* at 62.

³⁵⁸ *Id.* at 63.

³⁵⁹ *Id.* at 63–64.

³⁶⁰ *Id.* at 64.

³⁶¹ Luque-Vilchez & Larrinaga, *supra* note 356, at 62.

³⁶² *Id.* at 65.

³⁶³ *Id.* at 65.

For example, Costa and Agostini studied the effect of an Italian law covering the disclosure of environmental and labor issues that implemented the 2003 EU Directive.³⁶⁴ While they found an increase in the quantity of information disclosed, the quality of such reporting did not improve.³⁶⁵ Costa and Agostini concluded this was the result of two factors, namely (1) lack of focus on stakeholder engagement and institutional change in which an accountability mechanism was linked to the disclosure requirement and (2) the ambiguous nature of the disclosure mandate, which set forth overly broad and vague standards for non-financial reporting.³⁶⁶

In a study of the impact of France's NRE, Chauvey et al. concluded that the goal of increased transparency remained unmet.³⁶⁷ They examined changes in CSR disclosure by French companies over the time period from 2004 to 2010. The study noted that while there were increases in the quantity and breadth of disclosure by such companies, there was no improvement in informational quality.³⁶⁸ As a result Chauvey et al. determined that the NRE reporting requirements were moving in the direction of "normativity," namely viewed by actors as binding, but had not yet achieved that status.³⁶⁹ The results reported by Chauvey et al. are consistent with other studies conducted on the impact of Article 116 of the NRE, which studies were discussed in Section III.C above. Those studies also noted low quality of reporting, attributable to various factors including lack of reporting standards and ambiguities in the legal requirements,

³⁶⁴ Ericka Costa & Marisa Agostini, *Mandatory Disclosure about Environmental and Employee Matters in the Reports of Italian-Listed Corporate Groups*, SOC. & ENVTL. ACCOUNTABILITY J., 36:1, 10–33 (2016).

³⁶⁵ *Id.* at 12.

³⁶⁶ *Id.* at 30.

³⁶⁷ Jean-Noel Chauvey et al., *The Normativity and Legitimacy of CSR Disclosure: Evidence from France*, J. BUS. ETHICS 130:789–803, 801 (2015).

³⁶⁸ *Id.* at 800–801.

³⁶⁹ *Id.* at 801.

although over time the quantity of such reporting appears to have increased.³⁷⁰

Regarding the experience of Denmark, another EU Member State discussed in Section III.C above and an early adopter of mandated non-financial reporting, there is evidence that the amount of non-financial reporting increased as a result of the 2008 Act.³⁷¹ However, problems were reported with non-compliance by some companies, including inconsistencies in reporting and failure of auditors to note deficiencies.³⁷²

These empirical studies are relevant to an assessment of the 2014 EU Directive and can be read as calling into question the potential effectiveness of such Directive. This conclusion can be drawn from the fact that, although the Directive broadens the group of countries whose companies are now required to report CSR information, and although the Directive is more specific than the 2003 EU Directive in terms of the topics that must be covered and where such information should be presented, the “smart mix approach” of the 2014 EU Directive substantially weakens its mandate. In short, the 2014 EU Directive is not a strong mandate for non-financial reporting and does not seem that different from its predecessor Directive. There is little reason to think that the 2014 EU Directive will have a significant impact at this early stage of its implementation on the non-financial disclosure practices of business.

Although the empirical studies cited above relate to laws mandating non-financial reporting that predate the 2014 EU Directive, such studies suggest that new and updated laws put in place to implement such Directive by themselves may have only limited impact on CSR reporting practices. In explaining the lack of impact in the earlier time period, the authors of these studies cite various factors, including vague standards, lack of accountability or enforcement mechanisms, and lack of a shared

³⁷⁰ See *supra* notes 229–237 and accompanying text.

³⁷¹ See *supra* notes 274–288 and accompanying text.

³⁷² See *supra* notes 274–288 and accompanying text.

understanding of CSR, among other things. Some studies have focused on lack of stakeholder engagement and the problem of “normativity,” namely the failure of actors to see rules as binding. The issue of normativity was noted in the Chauvey et al. study of the impact of the NRE in France and has been mentioned in other studies in the sustainability accounting literature.³⁷³ To take another example, Bebbington et al. reported in their comparative study of non-financial reporting regimes in Spain and the United Kingdom that “formal legislation alone may not be sufficient to create a norm.”³⁷⁴ Other prerequisites for the legitimacy of norms must also be present in order for the norm to take hold and be widely accepted. This was the explanation offered by the authors of that study for the failure of full compliance with a mandated environmental reporting regime in Spain compared to the wide acceptance of a set of voluntary environmental reporting norms in the electric industry in the United Kingdom.³⁷⁵ To put it another way, a government mandate may not be a sufficient condition for a norm to be widely accepted and complied with.

Some of the other necessary conditions that might be required before the 2014 EU Directive achieves its desired effects could include the following: stronger and clearer standards regarding both the content of, and the framework for, non-financial reporting, enumerated sanctions for failure to comply with the reporting mandate, and a requirement of independent third party verification of the truthfulness of company disclosures, among other things.

Another challenge to the effectiveness of the 2014 EU Directive is the opposition by some sectors of the business community to a strong government mandate on non-financial reporting. It is reported in the literature that the original wording of the draft Directive was watered down in several important respects in the course of negotiations in response to

³⁷³ See Chauvey et al., *supra* note 367.

³⁷⁴ Jan Bebbington, et al., *The Production of Normativity: A Comparison of Reporting Regimes*, ACCT. ORGS. & SOC'Y, 37(2), 78–94, 90 (2012).

³⁷⁵ *Id.*

such opposition.³⁷⁶ The result was the adoption of the “smart mix approach” that provided business with a large amount of flexibility on compliance with the terms of the Directive. Another result was the substitution of weakened language regarding the businesses covered by the requirement, the content and format of reports, and enforcement and verification mechanisms.

In order for the 2014 EU Directive to achieve its goals, changes will be needed on several fronts. First, the flaws in the 2014 EU Directive identified in this article should be addressed since they significantly weaken the Directive’s non-financial reporting mandate. Second, businesses opposing expanded non-financial reporting based on a cost-benefit analysis should rethink their calculations to take into account not just short-term, but also long-term gains. Businesses might also ask whether they are doing the right cost-benefit analysis if they fail to account for social costs and externalities attributable to lack of appropriate company policies on CSR issues. A revised view of cost-benefit analysis on this topic might convince businesses that their opposition is unwarranted. One commentator has suggested an alternative strategy in which business should look at non-financial reporting not as a cost, but as an investment in the long-term sustainability of a company.³⁷⁷ Third, the lack of clarity identified in Section II above surrounding the rationale for CSR policies generally and for non-financial reporting in particular will hamper the development of standards for non-financial reporting unless this topic is addressed by business, government, and civil society. This may be a long-term project but identifying the issue will help to foster better regulation around this important topic.

V. CONCLUSION

This article has analyzed the development of mandatory non-financial reporting in the EU through actions taken by the European Commission culminating in the 2014 EU Directive. It has also touched on the development of mandatory non-financial reporting in two Member States

³⁷⁶ Kinderman, *supra* note 198.

³⁷⁷ Hess, *supra* note 344.

that have been in the forefront of legal developments on this topic, France and Denmark, as well as their implementation of the 2014 EU Directive. These twin inquiries have yielded some insights into the development of non-financial reporting in Europe that may be useful to other countries seeking to promote CSR among their own businesses using a disclosure-based approach. The United States is an example of a country that lacks a coherent regulatory approach to the topic of CSR reporting, but that could benefit from studying the lessons learned from the 2014 EU Directive.

One lesson learned is that non-financial reporting is moving from a voluntary to a mandatory activity in Europe and that is because stakeholders perceive that the quantity and quality of voluntary reporting is insufficient to meet their needs. Another lesson is that some form of joint public-private coordination may be needed to enhance such reporting by business, such as the “smart mix approach” used in the 2014 EU Directive. However, it should be acknowledged that there may be problems with business co-opting the reporting mechanisms under such an approach in order to further their own interests rather than those of their stakeholders. Yet another lesson is that the process of improving non-financial reporting may take place only gradually over a period of years through an evolutionary process. Many intermediate legislative and other steps will need to take place before the goal of improved transparency on CSR issues is attained.

Will the 2014 EU Directive foster greater CSR reporting? The answer to that question is still unknown and will not be known until several reporting cycles under the new Member State legislation have passed. However, some of the empirical work on reporting trends under Member State laws mandating non-financial reporting that predate the 2014 EU Directive concluded that the quantity of such reporting may have increased as a result. This suggests that companies may be expected to attempt compliance with national laws implementing the Directive and that we will see more non-financial reporting as a result. What is less clear is whether there will be any improvement in quality of reporting. The same empirical work just referred to above concluded that while there may have been some increase in the quantity of reporting after some national laws were enacted, the quality of non-financial reporting did not improve. This

suggests that any new laws or any amended laws that are enacted to implement the 2014 EU Directive will not necessarily improve the quality of reporting unless some specific guidance is given about the content of such reporting. Since the 2014 EU Directive does not mandate either the reporting standard or the format for such disclosure, allowing considerable flexibility to Member States on this issue, it seems unlikely that overall reporting quality will increase. In addition, there are other flaws in the 2014 EU Directive that have been identified in this article, such as the limitation on the enterprises that are covered by the Directive, the lack of penalties and enforcement mechanisms, and the lack of a third party verification of the truthfulness of disclosures. These weaknesses may impede achievement of the policy goals behind the 2014 EU Directive.

Will the 2014 EU Directive foster improved corporate performance on CSR measures? The answer to this question is even less clear, because improved performance is not a focus of the 2014 EU Directive. The 2014 EU Directive mandates reporting but it does not include a requirement that the Member States include benchmarking requirements for business in their implementing legislation or that they otherwise tie in such reporting with their financial reporting.³⁷⁸ As critics of the movement toward non-financial reporting as a regulatory mechanism for CSR have pointed out, non-financial reporting and achieving sustainability in business are separate concepts and triple bottom line reporting alone may not be a sufficient condition for achieving sustainability.³⁷⁹ This question raises the much larger issue of the best way to promote CSR and whether a disclosure-based approach is a better alternative than substantive regulation of corporate conduct.

At this point in time, there are still many other unanswered questions that remain about the future of mandatory non-financial reporting as an effective regulatory mechanism. In the EU, future research will be needed to assess the impact of the 2014 EU Directive and its implementation by Member States and to determine if the approach taken will yield

³⁷⁸ See 2014 EU Directive, *supra* note 12.

³⁷⁹ Markus Milne & Rob Gray, Whither Ecology? *The Triple Bottom Line, the Global Reporting Initiative, and Corporate Sustainability Reporting*, J. BUS. ETHICS 118:13-29, 14 (2013).

positive results for business and for society as a whole. The “smart mix approach” of the 2014 EU Directive may certainly be viewed as a useful intermediate step beyond voluntary disclosure that will foster a higher level of corporate disclosure, but further refinements will likely be needed if the policy objectives of such Directive are to be achieved. The form that such improvements should take will emerge as covered companies start to report under national laws adopted pursuant to the 2014 EU Directive and the “smart mix approach” is tested against the needs and demands of corporate stakeholders.