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Directors duties and human rights impacts: a comparative approach

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ABSTRACT
This article provides a comparative perspective on the issue of directors' liability for actions by a company which causes or contributes to human rights impacts. International, European and national regulatory developments in business and human rights are influencing company law. This article will consider directors' duties in relation to the meaning of 'the best interests of a company' and how the expectations on directors from various stakeholders are changing due to legislation, court decisions and practice. Based on this, there is an analysis of the link between directors' duties and human rights due diligence, and about access to remedy for the victims of actions arising from the acts or omissions of directors, including any decisions made by directors without proper regard for the human rights of those affected by the company's activities. It considers what might be the personal liabilities of directors in this area and possible ways forward, including in relation to probable EU regulation on this area.

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1. Introduction

On 29 April 2020, the European Commission announced its intention to legislate for cross-sectoral mandatory human rights and environmental due diligence requirements on companies.[1] In making this statement, the European Commissioner for Justice also stated:

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[1]EU Parliament Working Group on Responsible Business Conduct, 'Speech by Commissioner Reynders in RBC webinar on due diligence', 30 April 2020 <https://responsiblebusinessconduct.eu/wp/2020/04/30/speech-by-commissioner-reynders-in-rbc-webinar-on-due-diligence/> (EC Commissioner Speech).

> Besides the corporate due diligence duty, the duty of care of directors is also important, as it encourages them to integrate stakeholders' interests into corporate decisions alongside the interests of shareholders, to embed sustainability into corporate strategies and to adopt science-based targets.[2]

Since that time, the European Commission has clarified that legislative reform would have:

> [A]ims to ensure that sustainability is further embedded into the corporate governance framework with a view to align better the long-term interests of management, shareholders, stakeholders and society. It aims at improving the framework to incentivise corporate boards to integrate properly stakeholder interests, sustainability risks, dependencies, opportunities and adverse impacts into strategies, decisions and oversight.[3]

Such legislative action in the European Union (EU) would be a significant step in relation to both directors' duties generally and to those who suffer adverse human rights impacts from a company's activities.

This article will consider how the existing duties of directors might be affected if human rights due diligence were to become a mandatory obligation for companies (with sufficiently serious consequences in terms of sanctions in the event of breach). It will examine whether such a change could result in directors monitoring more proactively how companies identify and manage their human rights impacts, and will offer a comparative perspective (being primarily across the EU) on the issue of possible directors' liability for actions by a company which causes or contributes to human rights impacts.

In considering these possible effects, this article places this proposal by the European Commission within the context of both corporate law, which provides a regulatory framework for companies and directors, and the developments in business and human rights regulation. These developments have grown since the UN Guiding Principles on Business and Human Rights 2011 (UNGPs) established that States have legal obligations with regard to the human rights impacts of companies and that, separately, corporates have a responsibility to respect human rights and to remediate the human rights impacts of their activities.[4] While the UNGPs are not legally binding on States or companies, they have been deeply influential and have been adopted by States in international instruments, including binding treaties,[5]

[2]ibid (emphasis in original).
[3]EU Initiative on Sustainable Corporate Governance, Ref. Ares(2020)4034032 – 30/07/2020 <https://ec.europa.eu/info/law/better-regulation/have-your-say/initiatives/12548-Sustainable-corporate-governance>.
[4]United Nations Office of the High Commissioner for Human Rights, 'Guiding Principles on Business and Human Rights: Implementing the United Nations "Protect, Respect and Remedy Framework"' <www.ohchr.org/Documents/Publications/GuidingPrinciplesBusinessHR_EN.pdf>.
[5]See, for example, the Organisation for Economic Cooperation and Development Guidelines for Multinational Enterprises 2011 (OECD Guidelines) and the International Labour Organisation's Tripartite Declaration of Principles concerning Multinational Enterprises and Social Policy 2017.

national legislation and government policy statements,[6] and by industry sectors[7] and individual companies.[8] In particular, the UNGPs set out the concept of human rights due diligence as part of the corporate responsibility to respect human rights, by which a company should 'identify, prevent, mitigate and account for' actual or potential adverse human rights impacts that it may be involved in through its own activities (where it causes or contributes to an impact) or business relationships (where it is directly linked to an impact, including in its supply chain).[9]

Indeed, these developments in business and human rights clearly influenced the proposal by the European Commission. In his statement referred to above, European Commissioner for Justice, Didier Reynders, expressly relied on a Study produced for the European Commission on human rights and environmental due diligence in the supply chain (of which one of the authors of this article was a co-author).[10] Such proposals for legislative change at the EU level are important for our article. A second study was also produced for the European Commission on directors' duties and sustainable corporate governance,[11] yet most of its focus was on 'short-termism' in corporate governance and it has been heavily criticised.[12]

This article will begin by briefly clarifying what directors' duties are, to whom they are owed and who can bring an action when such duties are breached (and for what claim) by reference primarily to European developments and the laws in EU Member States. This approach is not intended to be

[6]See, for example, French Duty of Vigilance Act 2017 and the UK's National Action Plan on Business and Human Rights, both of which are discussed below. See also UK Home Office, *Transparency in Supply Chains etc. A Practical Guide* (Oct 2017), which refers directly to the UNGPs and human rights due diligence: <https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/649906/Transparency_in_Supply_Chains_A_Practical_Guide_2017.pdf>.

[7]See, for example, the statements by the International Council of Mining and Metals (ICMM): <www.icmm.com/en-gb/society-and-the-economy/mining-and-communities/human-rights>.

[8]See, for example, Unilever, Human Rights Policy Statement, <www.unilever.com/Images/unilever-human-rights-policy-statement_tcm244-422954_en.pdf>.

[9]UNGPs, Guiding Principle 15. For a fuller discussion of human rights due diligence, see Jonathan Bonnitcha and Robert McCorquodale, 'The Concept of "Due Diligence" in the UN Guiding Principles on Business and Human Rights' (2017) 28 *European Journal of International Law* 899.

[10]Lise Smit, Claire Bright, Robert McCorquodale, Matthias Bauer, Hanna Deringer, Daniela Baeza-Breinbauer, Francisca Torres-Cortés, Frank Alleweldt, Senda Kara and Camille Salinier and Héctor Tejero Tobed for the European Commission DG Justice and Consumers, *Study on Due Diligence Requirements Through the Supply Chain*, 24 February 2020 <https://op.europa.eu/en/publication-detail/-/publication/8ba0a8fd-4c83-11ea-b8b7-01aa75ed71a1/language-en> (EC Study). See also a response to the Study by civil society: The European Coalition for Corporate Justice, EU Model Legislation on Corporate Responsibility to Respect Human Rights and the Environment (February 2020) <https://corporatejustice.org/publications/eu-model-legislation-on-corporate-responsibility-to-respect-human-rights-and-the-environment/>.

[11]See EY, Study on Directors' Duties and Sustainable Corporate Governance (2020) <https://op.europa.eu/en/publication-detail/-/publication/e47928a2-d20b-11ea-adf7-01aa75ed71a1/language-en>.

[12]There was an EC consultation on this EY Study, which was open until October 2020, with some strong criticism of it, such as <https://ec.europa.eu/info/law/better-regulation/have-your-say/initiatives/12548-Sustainable-corporate-governance/F594640>.

comprehensive of all EU jurisdictions but it offers a cross-section of jurisdictions in order to highlight the selection of relevant issues raised. A comparative study can be taken in this area of law because legal duties on directors of companies – as duties of care and of loyalty – exist across all EU Member States.[13] Most of these are provided for in legislation, though some arise from decisions of courts, and these are largely consistent across all Member States:

> [T]he difference between common law and civil law, or between legal families, seems to have lost much of its relevance as corporate law reforms benefit from mutual learning and legal concepts are diffused internationally even without harmonisation efforts at [the] European level.[14]

The same authors note that some jurisdictions set out directors' duties precisely and specifically, while others are more general, and these variances are irrespective of their civil or common law tradition. This general harmonisation means that there is a considerable degree of similarity in the approach to directors' duties across the EU. Where there is divergence in the national laws of Member States regarding directors' duties, this partly arises from the different company board structures that exist.[15] In general, the Member States of the EU have two types of company board structures:[16] two-tier, where a company has two distinct boards, one with purely supervisory functions and a management board responsible for the organisation's day-to-day management; and one-tier, where the two functions are exercised by a unified board.[17] In all types of structures, the duties of directors are essentially the same.[18]

However, the proposed EU legislation is based on a criticism of current company law:

> Though (national) company laws in essence require corporate boards to act in the interest of the company *as a whole*, the company interest and directors duties are interpreted narrowly favouring maximisation of short-term financial value. Shareholder pressure also plays a role as well as directors' remuneration linked to financial performance. This market failure has been facilitated by shortcomings in corporate legislation and governance codes as they foster directors' accountability towards shareholders and do not sufficiently cover

[13]See, for example, Germany Companies Act, Article 93 (1) and UK Companies Act, section 174.

[14]Carsten Gerner-Beuerle and Edmund-Philipp Schuster, 'The Evolving Structure of Directors Duties in Europe' (2014) 15 *European Business Organization Law Review* 191, 199.

[15]For the difficulties in creating one 'European company', see the series by Dirk van Gerven and Paul Storm (eds) *The European Company* (CUP, 2006–2008).

[16]There is a separate 'Nordic' model which the authors do not address in this article for the sake of simplicity.

[17]There are some variations on this, which are not relevant for our purposes: see Gerner-Beuerle and Schuster (n 14) 195–96 and O. Sandrock and J. du Plessis, 'The German System of Supervisory Codetermination by Employees' in JJ du Plessis and others, *German Corporate Governance in International and European Context* (2nd edn 2012) chapter 5.

[18]German Companies Act, Article 116: 'the duty of care and responsibility of members of the management board shall … apply analogously to the duty of care and responsibility of the members of the supervisory board'.

> the interest of other stakeholders, including those affected by the company and the local and global environment.[19]

The article will consider aspects of the proposals in light of an examination of the meaning of 'the best interests of a company' and how the expectations on directors from various stakeholders are changing by legislation, courts and practice. These are necessary to include as they form the basis for the analysis of the link between directors' duties and human rights due diligence. They also enable consideration of access to remedy for the victims of actions arising from the acts or omissions of directors, including any decisions made by directors without proper regard for the human rights of those affected by the company's activities. The article concludes by considering what might be the personal liabilities of directors in this area and possible ways forward.

2. Directors' duties

If there is to be an EU-wide mandatory human rights and environmental due diligence requirement on companies and a change to the focus on sustainability by companies, then the comment from Commissioner Reynders above may suggest that the Commission also anticipates a new duty on directors to ensure companies take steps to comply with the law. However, even without the creation of a new duty on directors, directors may be required to exercise their existing legal duties to oversee a company's compliance with the new law, if non-compliance with the law triggers sufficiently serious consequences for the company.

This raises the issue as to whom the director's duty is currently owed under the law of Member States. The core aspect of the duty of a director is that the duty is generally *owed to the company*. There are usually considered to be three main corporate governance approaches as to what is the company to whom the duty is owed: to the shareholders as owners; to the stakeholders; and to the shareholders with some consideration of other stakeholders. The first approach is seen in Irish (and United States) company law;[20] the second approach (sometimes known as 'pluralist') is found in EU jurisdictions where employee representatives are on the board;[21] and the third approach (known as 'enlightened shareholder

[19]EC Sustainable Corporate Governance (n 3).

[20]On Ireland, see Brian Conroy, *The Companies Act 2014: An Annotation* (Round Hall 2015) 330–31.

[21]See Carsten Gerner-Beuerle, Philipp Paech and Edmund-Philipp Schuster, *Study on Director's Duties and Liabilities* (European Commission 2014) <http://eprints.lse.ac.uk/50438/1/__Libfile_repository_Content_Gerner-Beuerle, C_Study on directors' duties and liability(lsero).pdf>, who provide specific examples of state legislation across the EU and conclude (page vii): '[d]ifferences in board structures can have a significant impact on both the extent and content of directors' duties and liabilities, as well as on the enforcement of these duties'.

value') is seen in section 172 of the UK Companies Act.[22] Section 172 provides:

(1) A director of a company must act in the way he considers, in good faith, would be most likely to *promote the success of the company for the benefit of its members as a whole*, and in doing so have regard (amongst other matters) to –
  (a) the likely consequences of any decision in the long term,
  (b) the interests of the company's *employees*,
  (c) the need to foster the company's business relationships with *suppliers, customers and others,*
  (d) the impact of the company's operations on the *community and the environment,*
  (e) the desirability of the company maintaining a *reputation for high standards* of business conduct, and
  (f) the need to *act fairly* as between members of the company.
(2) Where or to the extent that the purposes of the company consist of or include purposes other than the benefit of its members, subsection (1) has effect as if the reference to promoting the success of the company for the benefit of its members were to achieving those purposes.
(3) The duty imposed by this section has effect subject to any enactment or rule of law requiring directors, in certain circumstances, to consider or act in the interests of creditors of the company.[23]

This section sets out quite a detailed set of statutory duties, which requires the consideration of the broader interests of a wide-range of stakeholders, including employees, suppliers, customers and the community, and interests such as the environment and the company's reputation. These interests of stakeholders are, though, within the context of the overall duty of directors to 'promote the success of the company for the *benefit of its members* as a whole', with those 'members' being the shareholders of the company.[24]

Therefore, the core aspect of the duty of a director is that the duty is in most circumstances owed to the company, even if these different corporate governance approaches offer different accounts as to what comprises the company.[25] In all three approaches above, the duty is to the company even if the interests of some or all stakeholders should be considered in the exercise of the director's activities. Therefore, as discussed below, a breach of this duty by a director may give rise to a civil claim by the company against the director.

[22]See Sarah Worthington, 'Reforming Directors' Duties' (2001) 64 *Modern Law Review* 439.
[23]UK Companies Act, section 172 (emphasis added).
[24]See UK Companies Act, section 112.
[25]See, for example, Ireland Companies Act 2014, section 224 and Spain Royal Legislative Decree 1/2010.

There is one situation across the EU in which this position changes: insolvency. Where the company is insolvent (or in the vicinity of insolvency) the directors owe a duty to the company's creditors. This is because:

> The shift in duty is a form of creditor protection, inhibiting companies externalising the cost of their debts at the time of financial distress. The reason for the duty is that if the company is in the vicinity of solvency or embarking on a venture, which it cannot sustain without relying totally on creditor funds, the interests of the company are in reality the interests of existing creditors alone.[26]

In general, a creditor in insolvency means the creditors as a whole and could include, for example, financial institutions, the government, employees, customers and suppliers.[27] Interestingly, the possibility of the duty of directors being to other stakeholders is left open in the expert group's guide for the United Nations Commission on International Trade Law (UNCITRAL).[28] This shift in the duty owed by directors does not enable a creditor to bring an action for the breach of a director's duty against a director. Rather, the directors' duties remain to the company, and any action would be on behalf of the company in the guise of the administrator or liquidator if the company is insolvent.[29]

3. Actions for breach of a directors' duty

The proposal by the European Commission acknowledges that one of its objectives is 'to increase corporate accountability for human and environmental harm'.[30] If such harm were to occur as a result of a breach of a directors' duty which in turn causes loss to the company (e.g. because the company incurs a heavy fine), then, as the director's duty is owed to the company, it is the company that could bring a claim against the directors.

A civil claim by shareholders against a company's directors will usually be brought on the company's behalf as a derivative action. A detailed comparative report by Dutch scholars affirms the position in the majority of cases:

> Case law established the notion that it is only the company that may claim a remedy where a wrong has been committed against it. Because a director's duties are owed to the company, and any loss resulting from breaches will be presumed to be losses to the company, it is the company which is the party primarily entitled to bring an action against the delinquent director.

[26]Andrew Keay, 'The Shifting of Director's Duties in the Vicinity of Insolvency' (2015) 24 *International Insolvency Review* 140, 144.

[27]For example, in the UK Insolvency Act 1986, section 382, a creditor can include those for whom there is unpaid wages or monies due to a supplier.

[28]UNCITRAL Legislative Guide on Insolvency Law, 'Directors' Obligations in the Period Approaching Insolvency' Working Group V <https://uncitral.un.org/en/texts/insolvency>. See also Irit Mevorach, 'The Role of Enterprise Principles in Shaping Management Duties at Times of Crisis' (2013) 14 *European Business Organization Law Review* 471. Review.

[29]See, for example, the UK Insolvency Act 1986, section 214.

[30]EC Commissioner Speech (n 1).

> The difficulty with this is that it is usually the people who are causing harm to the company that are also the ones controlling it .... Where the company cannot or will not sue that director, it is possible for one or more shareholders to bring proceedings to enforce a right of the Company. This is said to be deriving a right of action from the company, and is often referred to as a 'derivative claim'.[31]

In some Member States, shareholders are able to petition a public regulatory body to undertake an investigation into the company's affairs. For example, the Netherlands has an inquiry process where an investigator can undertake an inquiry into the policy and conduct of a company (and can suspend the directors, suspend voting rights and take similar actions) if so requested by a shareholder with at least 10% of the shares or of a value of €250,000.[32]

A shareholder that brings a derivative claim does so seeking relief on behalf of the company, rather than themselves, e.g. for negligence or a breach of duty on the part of one or more directors.[33] The claim is vested in the company, and the remedy sought is therefore to make good loss sustained by the company. This reflects the fact the directors' duties are owed to the company.

In some jurisdictions, however, a shareholder can bring a claim against directors on their own behalf for personal relief, either on unfair prejudice grounds[34] or, where special circumstances exist, for the breach of a fiduciary duty owed by the director directly to the shareholder.[35] Such personal claims by shareholders against directors are exceptions to the general corporate law principle that directors act as agents of the company and so will not usually incur personal liability except to the company.

Ultimately, the special circumstances where a director may owe a duty to an individual shareholder are limited, reflecting the principle that 'directors of a company are not trustees for individual shareholders',[36] at least ordinarily.

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[31] Liesbeth Enneking and others, 'Duties of Care of Dutch Business Enterprises with Respect to International Corporate Social Responsibility' (2015) <www.business-humanrights.org/sites/default/files/documents/2531-summary_tcm44-644144.pdf> (English translation).

[32] The Netherlands Civil Code 1992, Articles 2:344–2:359. There is a similar provision in Austrian law (Austrian Stock Corporation Act, § 130(2) (where shareholder holding 10% of the capital can request an inquiry if the facts indicate a material violation of the law or the articles) and Lithuanian law (Lithuanian Civil Code, Art. 2.124). Gerner-Beuerle, Paech and Schuster (n 21), also include as an example, the German Stock Corporation Act, § 140(2), where they state that shareholder having 1% of capital can request an inquiry with the same proviso as under Austrian law).

[33] See for example UK Companies Act, Section 260.

[34] For example, a minority shareholder can bring an action under section 994 of the UK Companies Act where the conduct of the company's affairs has unfairly prejudiced their interests as a member of the company.

[35] In some Member States, this sort of direct shareholder claim is possible if there is a 'special relationship' between the company and the shareholders, being '*something over and above the usual relationship which a director had with shareholders*' (e.g. in small and closely held companies): *Sharp v Blank* [2015] EWHC 3220 (Ch), para 12.

[36] *Percival v. Wright* [1902] 2 Ch 421.

There is also the related public policy that directors should not be 'over-exposed to the risk of multiple legal actions by dissenting minority shareholders'.[37]

The result is that there are often significant challenges for shareholders in bringing claims against directors for a breach of duty, particularly where 'the principles to be applied … confer a discretion on directors'[38] when exercising their duties to the company. For example, in relation to section 172 of the UK's Companies Act, the subjective nature of the duty[39] means that:

> [I]t is very difficult to show that the directors have breached this duty of good faith, except in egregious cases or cases where the directors have, obligingly, left a clear record of their thought processes leading up to the challenged decision.[40]

This position was made clear in the case of *R (People & Planet) v HM Treasury*[41] before the English courts, concerning an application for judicial review of the policies adopted by the UK government with respect to the management of its investment in a bank (Royal Bank of Scotland – RBS), of which the government (as HM Treasury) was the majority shareholder after the global financial crisis. It was claimed that HM Treasury should have acted for the social good under its policies. In rejecting the claim and noting a risk of shareholders 'trying to press the [directors] beyond the limits of their own duties' through 'interventionist policy', the Court noted:

> The basic point is that decisions regarding the management of RBS will be matters for the judgment of directors of RBS. The policy adopted by HM Treasury is that UKFI [as the UK government shareholder] can properly seek to influence the Board of RBS to have regard to environmental and human rights considerations in accordance with the RBS Board's duty under section 172.[42]

This highlights the inherent difficulty that shareholders would face in connection with any derivative action on behalf of the company against the directors for a breach of section 172.[43]

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[37]See the judgment of Mummery LJ in *Peskin v Anderson* [2000] EWCA Civ 326, para 30.

[38]*Re Smith and Fawcett Ltd*, [1942] Ch 304, per Lord Greene MR.

[39]In parliamentary debates prior to the enactment of the Companies Act, Attorney General Lord Goldsmith stated the following in relation to section 172: '[I]t is for the directors … to judge and form a good faith judgment about what is to be regarded as success for the members as a whole … they will need to look at the company's constitution, shareholder decisions and anything else that they consider relevant in helping them to reach that judgment.' Hansard, House of Lords, Volume 678, Column 256, 6 February 2006. See here: <https://publications.parliament.uk/pa/ld200506/ldhansrd/vo060206/text/60206-29.htm>.

[40]Paul Davies and Sarah Worthington, *Gower and Davies Principles of Modern Company Law* (9th edn 2012) 543 (latest edition not available to authors during Covid restrictions).

[41]*R (People & Planet) v HM Treasury* (2009) EWHC 3020.

[42]ibid, para 35. See also the Finland Supreme Court Decision KKO 2016:58, concerning whether corporate management could be held liable for environmental degradation by neglecting their obligations as members of the board of directors.

[43]Georgina Tsagas, 'Section 172 of the Companies Act 2006: Desperate times call for soft law measures' in N. Boeger and C Villiers (eds), *Shaping the Corporate Landscape: Towards Corporate Reform and Enterprise Diversity* (Hart Publishing 2018) 131.

Nevertheless, it is clear that directors will not be afforded unlimited discretion in their decision-making when discharging their duties. For example, directors that fail to undertake sufficient enquiries for the purposes of exercising oversight over the company, including by not procuring the necessary information to inform their decision-making, may be unable to show that their conduct met the requisite duty of care.[44] Under US law, the Delaware courts have held that, in order to prove a derivative claim that directors breached their duties to the company, the shareholder claimants had to prove:

> (1) that the directors knew or (2) should have known that violations of law were occurring and, in either event, (3) that the directors took no steps in a good faith effort to prevent or remedy that situation, and (4) that such failure proximately resulted in the losses complained of.[45]

However, such derivative claims based on an alleged failure by directors to oversee the company's operations impose an 'onerous pleading burden'[46] on shareholder claimants, and has been characterised by the Supreme Court of Delaware as 'possibly the most difficult theory in corporation law upon which a plaintiff might hope to win a judgment'.[47] Nevertheless, it is possible that the fact that shareholders may file a derivative suit may cause a deterrent effect or spur directors to implement greater monitoring and reporting oversight,[48] as is discussed below.

4. Best interests of the company

If questioned about the veracity or sufficiency of a report or other corporate information published by the company and approved by the directors, the directors are likely to argue that they were using their judgement as to what was in 'the best interests of the company', so that they acted in 'good faith'. Most Member States enable this argument if the director can show that, for example, a decision was made based on appropriate information and they reasonably believed that it was in the best interests of the company.[49] This is a subjective belief where the directors 'exercise their discretion bona fide in what they consider – not what a court may consider – is

[44]See also the commentary below regarding *Antuzis v DJ Houghton* [2019] EWHC 843 (QB): the case indicates that a claim for a breach of directors' duties may be easier to establish where the director deliberately causes the company to breach obligations owed to certain stakeholders where those obligations are underpinned by statute (e.g. a contractual obligation to pay employees the minimum wage).

[45]*In re Caremark International Derivative Litigation* 698 A.2d 959, 971 (Del. Ch. 1996).

[46]*Marchand v. Barnhill*, No. 533, 2018 (Del. June 18, 2019).

[47]*Stone v Ritter*, 911 A.2d 362, 372 (Del. 2006).

[48]See Laura Ezell, 'Human Trafficking in Multinational Supply Chains: A Corporate Director's Fiduciary Duty to Monitor and Eliminate Human Trafficking Violations' (2016) 69 *Vanderbilt Law Review* 499.

[49]See, for example, Finland's Limited Liability Companies Act 2006, Chapter 22 Section 1 and Italy's Civil Code, Article 2392.

in the interests of the company'.[50] For example, the provisions of section 172 of the UK Companies Act elaborating on the directors' duty to take into account a range of social and environmental factors are subject to the overarching principle that a director must 'act in the way he considers, in good faith, would be most likely to promote the success of the company for the benefit of its members as a whole'. No definition of 'success' is given, though it seems clear that it cannot be determined by reference only to the majority shareholders.[51]

However, developments in the elaboration of directors' duties mean that these arguments are not as conclusive as they may first appear. For example, Dutch listed companies are subject to the Corporate Governance Code, which is a code of conduct which should be included in their annual reports or else they have to explain why they were not included ('the apply or explain principle'),[52] as is the case in some other Member States.[53] This Dutch Governance Code includes social and environmental issues, as does the Spanish Good Governance Code.[54] Further, the Foreword to the German Corporate Governance Code provides:

> The Code highlights the obligation of Management Boards and Supervisory Boards – in line with the principles of the social market economy – to take into account the interests of the shareholders, the enterprise's workforce and the other groups related to the enterprise (stakeholders) to ensure the continued existence of the enterprise and its sustainable value creation (the enterprise's best interests).[55]

Although this statement is only found in the Foreword of the current version of the German Corporate Governance Code and not in the German Act on public limited companies [*Aktiengesetz*], it is nevertheless a significant statement about the importance of stakeholder interests. The Code itself states that '[t]he Management Board is responsible for managing the enterprise in its own best interests'.[56] This statement mirrors the wording of the

[50] *Re Smith & Fawcett Ltd*, [1942] 1 Ch 304 at 306 (per Lord Greene MR) and see *KeyMed (Medical & Industrial Equipment) Ltd v Hillman and Woodford* [2019] EWHC 485 (Ch) per Marcus Smith J.

[51] UK Department of Trade and Industry, Ministerial Statements, Companies Act 2006, Duties of Company Directors (2007) 7–8: 'the duty is to promote the success for the benefit of the members as a whole – that is, for the members as a collective body – not only to benefit the majority shareholders, or any particular shareholder or selection of shareholders'.

[52] For a detailed discussion see Enneking and others (n 31).

[53] See, for example, Ireland, 2017 Regulations implementing the EU Directive on Non-Financial Reporting and the Irish Human Rights and Equality Commission Act 2014.

[54] Spain Good Governance Code for Listed Companies 2013, Principle 24.

[55] German Corporate Governance Code 2020, Foreword. The Code applies to listed companies and compliance with it is not mandatory. German Company Law also includes a reference to 'sustainable development' in section 87 (1) 2: 'The remuneration system of listed companies shall be aimed at the company's sustainable development'. See, more generally, the excellent report in the EC Study by Daniel Augenstein on Germany Country Report, note 10, on which we rely.

[56] German Corporate Governance Code 2020, a Management of the Company, I Governance Tasks of the Management Board, Principle 1. Note that these Principles, according to the Code's Foreword, 'reflect

German Act on public limited companies, which provides in section 76(1): 'The management board shall have direct responsibility for the management of the company'.

However, it is important to consider that the previous version of the German Corporate Governance Code (2017) provided the following:

> The Management Board assumes full responsibility for managing the company in the best interests of the company, meaning that it considers the needs of the shareholders, the employees and other stakeholders, with the objective of sustainable value creation.[57]

That statement about the duties of the management board in the 2017 version of the Code is significant insofar as, according to its wording, it is intended to offer 'descriptions of statutory requirements and explanations'.[58] Yet the wording in the 2020 German Corporate Governance Code is silent on the issue, as is the Act itself. However, the wording of the Foreword, quoted above, is consistent with the text of the previous Code provision 4.1.1., in that there is no priority for any one group of stakeholders and, in particular, no priority expressly given to shareholders.

The background to all of this is that section 76(1) of the Act has been the basis for a long-standing debate about whether or not directors of German public limited companies have to pursue the interests of all stakeholders. The dominant view is that this section is to be interpreted in the way that directors are under no obligation to prioritise shareholder value and, instead, have to decide on a case by case basis what is in the best interest of the company, bearing in mind that they have to run the company in a profitable way. Based on this, Andreas Rühmkorf insightfully concludes:

> [A]t present, German company law certainly does not create a barrier to the promotion of sustainable development in that it does not require a prioritisation of shareholder value. Directors can therefore balance the interests of employees, the public and shareholders. This provides them with scope to pursue other interests than those of the shareholders. However, whilst this provides some opportunity for the promotion of sustainable development, the issue remains to what extent the interests of other stakeholder groups such as the environment, local communities, employees of suppliers need to be included in this process.[59]

material legal requirements for responsible governance, and are used here to inform investors and other stakeholders'.

[57] German Corporate Governance Code 2017, 4.1.1.

[58] See, more generally, Beate Sjåfjell and Benjamin J. Richardson, *The Future of Company Law and Sustainability'* (CUP 2015).

[59] Andreas Rühmkorf, 'Opportunities and Limitations for the Promotion of Sustainable Development in German Law' in Andreas Rühmkorf (ed), *Nachhaltige Entwicklung im deutschen Rech* (Nomos Verlagsgesellschaft 2018).

This German model has been called a 'moderate stakeholder approach [in contrast with] a shareholder approach' in determining the best interests of a company.[60] Any change in prioritisation between shareholders and other stakeholders would need to be by express terms in legislation in order to ensure that directors are clear as to their duties.[61]

Further, a major work by scholars seeking to clarify company law across the EU has stated that maximising profits is not a legal duty of directors:

> Contrary to widespread belief, *corporate directors generally are not under a legal obligation to maximise profits for their shareholders*. This is reflected in the acceptance in nearly all jurisdictions of some version of the business judgment rule, under which disinterested and informed directors have the discretion to act in what they believe to be in the best long term interests of the company as a separate entity, even if this does not entail seeking to maximise short-term shareholder value. Where directors pursue the latter goal, it is usually a product not of legal obligation, but of the pressures imposed on them by financial markets, activist shareholders, the threat of a hostile takeover and/or stock-based compensation schemes.[62]

Indeed, the Canadian Supreme Court has stated that, in considering the company's best interests, directors may look to the interests of 'shareholders, employees, creditors, consumers, governments and the environment to inform their decision'.[63]

It is also relevant that a director's duties arise in relation to the purpose of the company, as the director must act within those purposes, as seen above. These purposes can be separate from shareholder demands or solely profit-making.[64] Whether a company has a social purpose is a current matter of considerable debate (and beyond this article).[65] It is, though, relevant that a major investor has insisted that 'profits are in no way inconsistent with

[60]von Werder in Kremer and others (eds), *Deutscher Corporate Governance Kodex Kommentar* (6th edn, C.H. Beck 2016) 2 [Commentary on German Corporate Governance Code 2017], where the quotation is about the 2017 law, though, as noted above, it remains apt.

[61]For example, In France, a law setting out these priorities, Loi Pacte [*Projet de loi relatif à la croissance et la transformation des entreprises*], was adopted on 11 April 2019 but is not yet in force: <www.assemblee-nationale.fr/dyn/15/textes/l15t0258_texte-adopte-provisoire.pdf>. Article 169 amends the Civil Code and the Commercial Code to provides that a company is managed in its corporate interest while 'taking into consideration the social and environmental stakes of its activities'. However, the lack of a clear hierarchy between these potentially competing considerations has not given any clarity to companies and delayed its entry into force.

[62]Stout and others, 'Summary of Fundamental Rule of Corporate Law' in *The Modern Corporation Statement on Company Law* <https://commons.allard.ubc.ca/cgi/viewcontent.cgi?article=1418&context=fac_pubs#:~:text=%22The%20Modern%20Corporation%20Statement%20on%20Company%20Law%3A%20Summary%3A,School%2C%20City%20University%2C%20London%20to%20support%20the%20Purpose> (emphasis added).

[63]*BCE Inc v 1976 Debentureholders* [2008] 3 SCR 560.

[64]British Academy, *Reforming Business for the 21st Century* (2019) 10–11. In the UK the Corporate Governance Code was amended in 2018 to now provide (Section 1, Principle B): that 'the board should establish the company's purpose, values and strategy and satisfy itself that these and its culture are aligned'.

[65]Some States have created companies with specific social purposes: see John Montgomery, 'Mastering the Benefit Corporation' *Business Law Today* (July 2016), at 1 and Alexandra Leavy, 'Necessity Is the

purpose – in fact, profits and purpose are inextricably linked', in its call for companies to acknowledge and act on their social purpose.[66] It is also notable that a major company, Danone, has changed its legal status to a purpose-driven company to benefit 'its customer's health and the planet'.[67]

Indeed, a recent review by the British Academy of the role of the company in society took a strong view about the public purpose of companies:

> Public purposes are particularly relevant to corporations that perform public functions. These include utilities, corporations with significant market power, private infrastructure providers, corporate partners in private finance initiatives and public private partnerships, and banks. There is a particularly strong case for aligning the purposes of these corporations with their public purposes. Elsewhere such alignments should be restricted to those aspects of corporate activities that raise particular public interests, in relation to, for example, corporate taxation, human rights and corruption.[68]

Accordingly, it is certainly arguable that interests other than those of the shareholders and maximising profits may be included within the purpose of a company and the duties of directors. This has been expanded upon by legislation and practice as will be considered in the next section.

5. Developing directors' duties by legislation

There have been a few pieces of legislation in Member States which have been inspired by the business and human rights regulatory developments,[69] in which directors' duties have been considered. Amongst the most focussed is the addition of sections 414A-C to the UK Companies Act in 2013, inserted 'to ensure that directors of quoted companies consider human rights issues when making their annual strategic reports'.[70] This statement was made in the UK government's National Action Plan on Business and Human Rights, being its commitment to the implementation of the UNGPs.

Section 414C(7) of the UK Companies Act[71] requires that the strategic report of a quoted company[72] include information about 'environmental

Mother of Invention: A Renewed Call to Engage the SEC on Social Disclosure' (2014) 2014 Columbia Business Law Review 463, 488.

[66]See Letter from Larry Fink, CEO of Black Rock in 2019: <www.blackrock.com/corporate/investor-relations/larry-fink-ceo-letter> and commentary: <https://globescan.com/analysis-larry-finks-annual-letter/>, and <www.thenation.com/article/archive/big-business-has-a-new-scam-the-purpose-paradigm/>.

[67]'Danone Adopts New Legal Status to Reflect Social Mission' *Financial Times* (26 June 2020): see <https://on.ft.com/2ZvRFJ0>.

[68]British Academy (n 64) 17.

[69]See EC Study (n 10).

[70]HMG, *Good Business: Implementing the UN Guiding Principles on Business and Human Rights* (National Action Plan on Business and Human Rights) Updated May 2016, 7.

[71]Inserted by the Companies Act 2006 (Strategic Report and Directors' Report) Regulations 2013 (S.I. 2013/1970).

[72]Under section 385(2) of the UK Companies Act, a 'quoted company' is defined as a company with equity share capital: (i) included in the Official List in accordance with Part VI Financial Services and

matters (including the impact of the company's business on the environment) [and] social, community and human rights issues … to the extent necessary for an understanding of the development, performance or position of the company's business'. Since 2019, 'large'[73] UK companies have also been required to include a 'section 172 statement' in their strategic reports describing how the directors have had regard to their duties under section 172 of during the financial year.[74] As noted above, section 172 requires directors to promote the success of the company for the benefit of its members as a whole, having regard to matters including the community, the environment and the company's reputation.

Thus, human rights issues (which are of sufficient significance to warrant reference in the strategic report) are to be specifically included in a strategic report or there may be a breach of the director's duty, being a duty to report in this instance, though bearing in mind that section 414C(1) states that '[t]he purpose of the strategic report is to inform members of the company and help them assess how the directors have performed their duty under section 172 (duty to promote the success of the company)'. Thus there is clearly an attempt to link directors' duties with the responsibility on companies to respect human rights under the UNGPs, and the associated expectation on companies to perform human rights due diligence.

However, section 414C of the UK Companies Act limits the necessary information (for the purposes of the strategic report, of which the section 172 statement forms a part) to that which gives a 'fair review' of the company's business (specifically its 'development and performance') as well as its 'principal risks and uncertainties'.[75] This has led the UK's Financial Reporting Council Conduct Committee to publish guidance (which is voluntary but intended to represent best practice)[76] concluding that only 'information that is material to shareholders should be included in the strategic report. Immaterial information should be excluded as it can obscure the key messages'.[77] This would appear to be a narrow and technical view, not in keeping with the UK government's intentions when introducing the above reporting requirements. Nevertheless, the current position is that there is no liability on directors for a failure to include human rights information in

Markets Act 2000; (ii) officially listed in an European Economic Area (EEA) State; or (iii) admitted to dealing on either the New York Exchange or Nasdaq.

[73]Under section 465 of the UK Companies Act, a 'large company' is one which meets two of the following three criteria: (i) a global turnover in excess of £36 million; (ii) a balance sheet in excess of £18 million; and (iii) more than 250 employees.

[74]UK Companies Act, Sections 414CZA, inserted by the Companies (Miscellaneous Reporting) Regulations 2018.

[75]UK Companies Act, Sections 414C(2) and (3).

[76]The UK's Financial Reporting Council has published Guidance on the Strategic Report (July 2018) 2 <www.frc.org.uk/getattachment/fb05dd7b-c76c-424e-9daf-4293c9fa2d6a/Guidance-on-the-Strategic-Report-31-7-18.pdf>.

[77]ibid 4.

the strategic report if they can show that the lack of this disclosure was not necessary for an understanding of the company's business.[78]

Another legislative development inspired by the UNGPs is the French Duty of Vigilance Act 2017.[79] It creates a duty of vigilance for harms caused by a company, including the activities of companies controlled directly or down the supply chain and the activities of subcontractors and suppliers 'with which the company maintains an established commercial relationship'.[80] In order to discharge this duty, companies need to implement a 'vigilance plan' which should include reasonable measures to adequately identify risks and prevent serious violations of human rights.[81] The duty under the legislation is on the company, not the directors directly, so it does not directly affect directors' duties. It is also restricted to a relatively small group of companies, being those registered in France with 5000 employees in France or 10,000 globally.

Subsequent legislation has taken these principles one step further to include personal liability. For example, the Dutch Child Labour Due Diligence Act 2019 creates a personal liability for the company's compliance officer (the role of which must be appointed) if there is no action by the company under the legislation.[82] It is possible that companies will designate a director as having responsibility for overseeing compliance, which could open possibilities for a breach of a director's duty, though the drafting appears to indicate that the compliance office is not intended to be a director. The Child Labour Due Diligence Act applies to all companies who sell products or services to Dutch consumers, whether incorporated in the Netherlands or not. More recently, the German Corporate Due Diligence in Supply Chains Act 2021 and the Norwegian Transparency Act 2021 both include mandatory human rights due diligence requirements on companies and arguably represent 'significant strides forward from non-financial reporting requirements'.[83]

[78]See section 414C(7). Similarly, the requirements to disclose information about modern slavery in a company's business under section 54 of the United Kingdom's Modern Slavery Act do not include any effective sanction for non-disclosure, with many companies not providing any clear detail; see, for example, Independent Anti-Slavery Commissioner & University of Nottingham: Rights Lab, *Agriculture and Modern Slavery Act Reporting: Poor Performance Despite High Risks: A Research Report from the Office of the Independent Anti-Slavery Commissioner and the University of Nottingham's Rights Lab* (2018) <www.antislaverycommissioner.co.uk/media/1220/modern-slavery-act-and-agriculture-poor-performance-briefing.pdf>.

[79]Law No. 2017-399 of 27 March 2017 on the 'Duty of Care of Parent Companies and Ordering Companies'.

[80]Sandra Cossart, Jérôme Chaplier and Tiphaine Beau De Lomenie, 'The French Law on Duty of Care: A Historic Step Towards Making Globalization Work for All' (2017) 2 *Business and Human Rights Law Journal* 317 at 320.

[81]ibid.

[82]On the Dutch Child Labour Due Diligence Act see Anneloes Hoff <http://ohrh.law.ox.ac.uk/dutch-child-labour-due-diligence-law-a-step-towards-mandatory-human-rights-due-diligence>.

[83]Markus Krajewski, Kristel Tonstad and Franziska Wohltmann, 'Mandatory Human Rights Due Diligence in Germany and Norway: Stepping, or Striding, in the Same Direction?' *Business and Human Rights Journal* | FirstView articles | Cambridge Core, 9.

The other piece of EU legislation that has specifically referred to human rights and environmental matters as part of the director's duties is the EU Non-Financial Reporting Directive ('NFR Directive'), which requires certain large public companies and financial corporations operating in the EU to disclose information on environmental, social, human rights and anti-corruption matters, necessary for understanding the company's development, performance, position and impact.[84] By December 2017 all EU Member States had transposed these rules into national legislation. Some, such as Denmark, France, Greece and Sweden, have extended the application to a wider range of companies than in the NFR Directive.[85] While most Member States require reporting on these matters in a separate statement, France and the UK require them to be included in a company's annual report.[86] However, the focus of the NRF Directive is on reporting by the directors and, arguably, '[b]y defining these issues as non-financial, or as concerning 'non-shareholder' interests, or as 'ethical' rather than 'economic', the message is clearly that these are extraneous concerns' to a director.[87]

Nevertheless, these non-financial reporting requirements can have an impact on companies. A report by the Alliance for Corporate Transparency analysed the non-financial statements of 105 companies from three sectors and six European regions and concluded:

> The analysis of the gathered data points consistently to one overarching conclusion. *The vast majority of companies acknowledge in their reports the importance of environmental and social issues*. However, more often than not this information is not clear in terms of concrete issues, targets and principal risks. The general information that most companies provide does not allow investors and other actors to understand companies' impacts and by extension their development, performance and position. The solution to this predicament is to enhance the specificity of the NFR Directive with regard to what companies should disclose.[88]

This is an important conclusion.

[84]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.

[85]See GRI, *Policy & Reporting: Member State Implementation of Directive 2014/95/EU* (2018) <www.globalreporting.org/resourcelibrary/NFRpublication%20online_version.pdf>.

[86]See Frank Bold, *Comparing the Implementation of the Non-Financial Reporting Directive* (2017) <www.purposeofcorporation.org/comparing-the-eu-non-financial-reporting-directive.pdf>. Note that under the French law, a company's obligations conflate with the board's obligations: see article L. 225-102 of the Code de commerce.

[87]Beate Sjåfjell, 'Beyond Climate Risk: Integrating Sustainability into the Duties of the Corporate Board' (2018) 23 *Deakin Law Review* 13.

[88]Alliance for Corporate Transparency, *The state of corporate sustainability disclosure under the EU Non-Financial Reporting Directive* (2019) 60 (emphasis added) <www.allianceforcorporatetransparency.org/assets/2018_Research_Report_Alliance_Corporate_Transparency-66d0af6a05f153119e7cffe6df2f11b094affe9aaf4b13ae14db04e395c54a84.pdf>.

6. Risks to the company

As noted in section 3 above, one option for the European Commission in developing its proposal for an EU-wide human rights and environmental due diligence law may be to promulgate legislation which carries with it a threat of a significant sanction for the company in the event of non-compliance, such as large financial penalties or debarment from public contracts. If this proposal was put into legislation, then the risk of non-compliance with the law by a company could be sufficiently material that, if a company took inadequate steps to comply with the law and the directors failed to exercise oversight in this regard, this would be a dereliction of the directors' duties under the law of the relevant Member State.

An example of how this approach may work can be seen in the German law context, which provides that all directors have a joint due diligence obligation to set up and supervise a firm-wide compliance system for damage prevention and risk control.[89] In 2013, a successful derivative action was brought against the directors of Siemens in Germany for their failure to implement an effective anti-bribery risk management system throughout the company's global operations.[90] In that case, the directors were in breach their due diligence obligations because they failed to establish a functioning compliance system that ensured the effective monitoring and control of business processes.[91] That obligation under German law extends to all of the company's subsidiaries, even if they are located abroad. The scope of the due diligence obligation is determined in view of the type, size and organisation of the company, the legal regulations to be complied with (in the case at hand, the prevention of bribes) and the risk of violations specific to the company.

A recent case in the UK courts concerning the mistreatment of workers suggests that a director may also breach their duty to act in a company's best interests by knowingly allowing it to engage in illegal, reputationally damaging conduct. Although the facts of the case are quite particular, *Antuzis v DJ Houghton* is interesting in the context of this article as companies often do suffer reputational damage if they are associated with human rights impacts or environmental harms. The Court held that directors of a company were personally liable for conduct amounting to modern slavery (involving breaches of the workers' contracts arising from non-compliance with UK

[89]See R Grabosch and C Scheper, *Die menschenrechtliche Sorgfaltsplicht von Unternehmen: Politische und rechtliche Gestaltungsansätze* (2015) 34–35, when considering section 91(2) of the Stock Corporation Act.

[90]*Neubürger case* (Regional Court Munich I, 10 December 2013–2015 HK 1387/10, NZG 2014, 345). The court held the member of the directors were liable for damages towards the Siemens company. A similar case was brought in Italy, though against the company: Trib.di Milano – ordinanza Gip Salvini (27 aprile 2004) Trib. di Milano – riesame (28 October 2004).

[91]LG München I, Urteil vom 10 Dezember 2013–5 HK O 1387/10 – Siemens/Neubürger.

legislation, including the National Minimum Wage Act 1998) and linked it to the directors' duties under section 172 of the UK's Companies Act.[92] The Court explained this as follows:

> There is, plainly, a world of difference between, on the one hand, a director consciously and deliberately causing a company to breach its contract with a supplier, by not paying the supplier on time because, unusually, the company has encountered cash flow difficulties, and, on the other hand, a director of a restaurant company who decides the company should supply customers of the chain with burgers made of horse meat instead of beef, on the basis that horse meat is cheaper. In the second example, the resulting scandal, when the director's actions come to light, would be, at the very least, likely to inflict severe reputational damage on the company, from which it might take years to recover, if it recovered at all. Accordingly, *as a general matter, the fact that the breach of contract has such a statutory element may point to there being a failure on the part of the director to comply with his or her duties to the company and, by extension, to the director's liability to a third party for inducing the breach of contract.* Whether such a breach has these effects will, however, depend on the circumstances of the particular case … .
>
> [Accordingly,] I find beyond doubt that [the defendants] acted in breach of sections 172 and 174. What they did was not in the best interests of the company or its employees. On the contrary … they wrecked its reputation in the eyes of the community.[93]

In the *Antuzis* case, the defendants (the only two directors of the company) were knowingly and intimately involved in the mistreatment of the workers. While this sort of factual matrix may be less common in the case of directors of large, multinational companies, the general principle applies that directors may breach their duties by their actions which negatively affect the company's reputation.

Similarly, certain human rights and environmental issues (most notably climate change) could be seen as entailing financial risk for corporations, and so directors might be considered to have not fulfilled their duties if they reject or ignore climate change.[94] Potentially there could be derivative claims against directors for negligent loss to the company, such as where a director fails to take action to cease carbon emissions or eliminate fossil fuel energy.[95]

There has been no testing of this in the UK or EU courts to date, other than cases against the State.[96] Yet there have been a few claims based on climate

[92]*Antuzis v DJ Houghton* [2019] EWHC 843 (QB).
[93]ibid, paras 120, 122 and 124 (emphasis added). The director's liability to a third party would arise, for example, if the director themselves agreed to the contract in their personal capacity.
[94]See Sarah Barker, 'Directors' Personal Liability for Corporate Inaction on Climate Change' (2015) 67(1) *Governance Directions* 21.
[95]See Ewan McGaughey, *Principles of Enterprise Law* (CUP 2022 forthcoming) chapter 11.
[96]See, for example, *Urgenda Foundation v The State of The Netherlands* <https://elaw.org/system/files/urgenda_0.pdf?_ga=2.177437221.1833704640.1556127508-277280738.1537882574>.

change risks in other jurisdictions. For example, in 2017 shareholders of the Commonwealth Bank of Australia brought a claim against its directors on the basis that their annual report did not adequately inform investors of climate change risks and they sought an injunction to stop the bank making the same omissions in future annual reports.[97] The claim was avoided when, a week later, a new report was published by the bank's directors in which it was stated that climate change posed a significant risk to the bank's operations.[98] There is also a claim in the Federal Court of Australia against a pension fund for failure to disclose information about the fund's strategies to deal with climate change.[99] There have also been a number of derivative actions against directors in the US on the basis of failure to account for and prevent environmental damage, such as against BP for explosions at oil refineries.[100]

In 2018, UK NGO ClientEarth filed complaints with the UK's Financial Reporting Council Conduct Committee against prominent insurers and FTSE100 companies (as well as their auditors) alleging that the companies' strategic reports (under sections 172 and 414C of the UK Companies Act) included insufficient detail regarding principal risks and uncertainties to their businesses as a result of climate change.[101] More recently, the Dutch OECD National Contact Point has mediated an agreed settlement of an action by some NGOs against ING, a financial institution, in which ING agreed to measure, set targets for and steer their indirect climate impact,[102] In May 2021, a Netherlands Court considered a case brought against Royal Dutch Shell (Shell) in relation to their legal obligations concerning climate change.[103] The court held that Shell had a duty of care (and in doing so relied directly on the UNGPs)[104] and decided:

> [T]he end-users of the products produced and traded by the Shell group are at the end of RDS' value chain. RDS' responsibility therefore also extends to the CO2 emissions of these end-users (Scope 3). This is in line with the analysis of the various protocols and guidelines for climate change for non-state actors,

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[97]See <www.theguardian.com/australia-news/2017/sep/21/commonwealth-bank-shareholders-drop-suit-over-non-disclosure-of-climate-risks>.

[98]ibid. The Bank also published its first climate policy position statement, saying it would target an average emissions intensity decrease of its business lending portfolio consistent with its commitment to a net zero emissions economy by 2050.

[99]See <www.abc.net.au/news/2018-07-25/super-fund-rest-sued-for-not-doing-enough-on-climate-change/10029744>. The fund responded that it considers *'environmental, social and governance (ESG) risks in order to deliver competitive long-term investment returns for our members*'.

[100]*In re BP plc Derivative Litig.*, 507 F. Supp. 2d 302, 303–05 (S.D.N.Y. 2007). It was dismissed on procedural grounds.

[101]See <www.documents.clientearth.org/library/download-category/company-reporting/>.

[102]The Netherlands OECD National Contact Point, Oxfam and others v ING, 19 April 2019, <https://www.oecdguidelines.nl/latest/news/2019/04/19/final-statement-dutch-ncp-specific-instance-4-ngos-versus-ing-bank>.

[103]*Milieudefensie v Royal Dutch Shell*, District Court of the Hague, 26 May 2021 <https://uitspraken.rechtspraak.nl/inziendocument?id=ECLI:NL:RBDHA:2021:5339>.

[104]ibid, para 4.4.11.

> drawn up by the University of Oxford in 2020 (hereinafter: the Oxford report) … . [I]t does follow from the Oxford report that, although there are nuances, it is internationally endorsed that companies bear responsibilities for Scope 3 emissions. The court has included this widely endorsed starting point in its interpretation of the unwritten standard of care. The court notes that the level of responsibility is related to the extent to which companies have control and influence over the emissions.[105]

While the court did not refer to director's liabilities, there is clear increased expectation for directors to take into account factors such as sustainability and climate change in their decision making.[106]

Moreover, the examples noted above demonstrate how a failure to consider properly such issues by a company's directors could, in certain circumstances, expose both the company and the directors to legal liability, as being a foreseeable, material and adverse impact on the company's financial interests An internal framework could be incorporated or augmented into the company's existing risk management systems (such as for health and safety and labour issues) to facilitate informed decision-making by the directors based on sufficient information gathered and then provided to the board by personnel with appropriate expertise. With the exception of smaller companies, directors will not logically be able to discharge their supervisory responsibilities without the implementation of such a system. Indeed, the German Administrative Offences Act authorises the competent public authority to impose fines on business owners for failure to comply with these types of monitoring and supervision obligations.[107] It is possible that the lack of taking into account these sustainability factors may open directors to a derivative claim that they are not acting in the best interests of the company. Indeed, investors are increasingly aware of this, as seen in the decision of Norway's sovereign wealth fund ceasing its investment in palm oil companies due to deforestation risks.[108]

7. Human rights and directors' duties

It is consistent with these developments in requiring directors to consider and report on human rights and environmental risks, that human rights risks could be seen to be part of a director's duties for which a lack of action by the directors might lead to a claim for breach of duty. For

[105] ibid, paras 4.4.18 <https://uitspraken.rechtspraak.nl/inziendocument?id=ECLI:NL:RBDHA:2021:5339>.

[106] Beate Sjåfjell, 'Dismantling the Legal Myth of Shareholder Primacy: The Corporation as a Sustainable Market Actor' *Nordic and European Company Law Paper* (2017), 7 argues (10): 'Generally, company law across jurisdictions also allows boards to integrate environmental externalities to a greater extent than legal compliance requires, at least as far as the business case argument allows – that is as far as the case can be made that this is profitable for the company in the long run'.

[107] Germany Administrative Offences Act 1986, Article 130.

[108] M. Taylor, 'Norway's Wealth Fund Ditches 33 Palm Oil Companies over Deforestation' (28 February 2019) <http://news.trust.org/item/20190228120400-6pean/>.

example, a claim was brought in the US alleging that directors failed in their duty to create an environment where no sexual harassment occurred, which led to a settlement with an agreement that the directors would put in place corporate governance reforms.[109]

In fact, the increase in litigation against companies for their activities that violate human rights is of relevance to directors' duties. There have been cases brought in France,[110] Germany,[111] the Netherlands[112] and the UK[113] against companies, often for actions by their subsidiaries or suppliers where there have been human rights or environmental impacts. For example, the UK Supreme Court in *Vedanta v Lungowe* held that a parent company may owe a duty of care to the victims of environmental damage and human rights impacts caused by the actions of a foreign subsidiary.[114] While these are all claims against companies, they do show that litigation and public reports linking a company to human rights violations may cause not only legal risks but also significant reputational damage to a company. Beyond that, companies associated with human rights or environmental issues may suffer significant financial damage, including lost sales, contracts or operating licences, exclusion from tenders, declines in share price value, and even insolvency.[115] It would seem possible that a lack of consideration of human rights risks could lead to (derivative) claims by shareholders against the company's directors for a breach of their directors' duties. Such claims would be underpinned by an allegation that the company suffered harm resulting from a failure by directors to consider properly the risks associated with a particular activity carried out by the company which led to (for example) environmental damage and the consequent revocation of the company's operating licence.

Lawsuits against directors for human rights abuses can include criminal charges. For example, in France the eight former directors of Lafarge have been charged under the French Criminal Code with complicity in war

[109] *City of Monroe Employees Retirement System v Murdoch*, Case No. 2017-0833 (Verified Derivative Complaint) (Delaware Chancery Court 20 November 2017) <https://ca.reuters.com/article/businessNews/idCAKBN1DK2NI-OCABS>. Our thanks to Suzanne Spears for these insights.

[110] For example, a case brought against Amesys (www.business-humanrights.org/en/amesys-lawsuit-re-libya-0) and French NCP, *DEVCOT: Communiqué of the French National Contact Point for the OECD Guidelines for Multinational Enterprises*, 21 September 2012. See also the summaries in Lara Blecher, 'Codes of Conduct: The Trojan Horse of International Human Rights Law?' (2016) 38 *Comparative Labor Law and Policy Journal* 437 at 462–64.

[111] For example, *Jabir v KiK Textilen und Non-Food GmbH* <https://www.business-humanrights.org/en/kik-lawsuit-re-pakistan>, which was dismissed for being beyond the relevant statute of limitations in Pakistan.

[112] For example, *Akpan v Royal Dutch Shell PLC* Arrondissementsrechtbank Den Haag, 30 January 2013 Case No C/09/337050/HA ZA 09-1580.

[113] For example, *Chandler v Cape Plc* [2012] EWCA Civ 525.

[114] *Vedanta Resources v Lungowe* [2019] UKSC 20.

[115] See, for example, the insolvency of Bell Pottinger due to its actions in South Africa, for which the directors may be personally liable: <www.msn.com/en-gb/finance/other/bell-pottinger-partners-could-face-legal-action-over-collapse/ar-BBW3IVu>.

crimes and crimes against humanity due to their actions in agreeing commercial agreements with the Islamic armed group (ISIS) in Syria, which endangered its employees and caused it to be complicit in abductions.[116] A trial has commenced in Italy against ENI's current CEO and a former director for international corruption allegedly committed in Nigeria.[117] In each case, the directors' duties to the company have not yet been brought into the claim.

These developments indicate that, while these situations of liability are uncommon at the moment, directors should be aware of the potential adverse consequences of ignoring human rights risks when considering the best interests of the company. It is certainly possible for directors to put in place effective and appropriate monitoring systems as a means to reduce these risks to the company and enable adequate disclosure of these risks.[118] Such monitoring systems should be applying human rights and environmental due diligence as part of the best practices by a company.[119] Further, it would now be difficult for most directors (particularly of larger companies) to be without some knowledge of human rights issues, especially where a company has subsidiaries and supply chains in sectors that are frequently associated with human rights issues in the media.[120] If there were a mandatory requirement for companies to conduct human rights due diligence then the board of directors would be expected to ensure that it was conducted by employees and contractors with appropriate expertise and with appropriate resources. Without such a mandatory due diligence requirement, it would be much more difficult to argue that the directors' duties extended to specific human rights monitoring systems.

8. Directors' duties and human rights due diligence

Taking account of these human rights risks by putting in place some monitoring systems – consistent with human rights due diligence – for evaluating risks to the company should have a positive effect on that company's operations, employees, suppliers, legal actions and its reputation. This is consistent with the decision in the US case of *Caremark*:

[116]See <www.business-humanrights.org/en/lafarge-lawsuit-re-complicity-in-crimes-against-humanity-in-syria>; and Historic victory before French Supreme Court on the indictment of multinational Lafarge for complicity in crimes against humanity – SHERPA.

[117]For publicly available documents and the point of view of NGOs <https://shellandenitrial.org/intro/>.

[118]See Laura Ezell, 'Human Trafficking in Multinational Supply Chains: A Corporate Director's Fiduciary Duty to Monitor and Eliminate Human Trafficking Violations' (2016) 69 *Vanderbilt Law Review* 499.

[119]For more detail, see Robert McCorquodale and others, 'Human Rights Due Diligence in Law and Practice: Good Practices and Challenges of Business Enterprises' (2017) 2 *Business and Human Rights Journal* 195.

[120]See discussion in Lise Smit and others, 'Human Rights Due Diligence in Global Supply Chains: Evidence of Corporate Practices to Inform a Legal Standard' (2021) 25 *International Journal of Human Rights* 945.

> [I]t would … be a mistake to conclude that … corporate boards may satisfy their obligation to be reasonably informed concerning the corporation, without assuring themselves that information and reporting systems exist in the organization that are reasonably designed to provide to senior management and to the board itself timely, accurate information sufficient to allow management and the board, each within its scope, to reach informed judgments concerning both the corporation's compliance with the law and its business performance.[121]

This decision reinforces the core elements of a director's duties in relation to oversight and advice to the management of a company. This decision was confirmed by the Delaware Supreme Court in *Marchand v. Barnhill*[122] in a case involving contaminated food. The Court stated that 'the board must make a good faith effort … to put in place a reasonable board-level system of monitoring and reporting'.[123] Accordingly, the Court held that, where the claim supports 'an inference that no system of board-level compliance monitoring and reporting existed' or was not implemented in good faith,[124] then the directors could be held liable.

This statement could be seen as a duty on a director to assess risks to the company, take action to monitor and operationalise the assessment of risks, track the effectiveness of the response to these risks, and then to communicate them internally and externally. Therefore, if directors have established an appropriate risk management system that enables them to identify, monitor and address risks, including human rights risks, then there would be limited circumstances (other than those discussed in the next section) in which directors might be considered be liable.

This is almost exactly what is meant by human rights due diligence, as Guiding Principle 17 of the UNGPs provides:

> In order to identify, prevent, mitigate and account for how they address their adverse human rights impacts, business enterprises should carry out human rights due diligence.

This connection is not unexpected, as the creation of the terminology of human rights due diligence was linked to business due diligence.[125] In a business context, due diligence is normally understood to refer to a process of investigation conducted by a business to identify and manage commercial risks, as:

[121] *In re Caremark International Derivative Litigation* 698 A.2d 959, 971 (Del. Ch. 1996).
[122] *Marchand v. Barnhill*, No. 533, 2018 (Del. June 18, 2019).
[123] ibid 30–31.
[124] ibid 36. See G. Pecht and others, 'The Delaware Supreme Court Clarifies the Standards for Director Oversight Liability Under *Caremark*' <www.nortonrosefulbright.com/en-us/knowledge/publications/4a67ec3e/the-delaware-supreme-court-clarifies-the-standards-for-director-oversight-liability-under-caremark>.
[125] For a more detailed discussion, see Bonnitcha and McCorquodale (n 9).

> [T]he main purpose [of due diligence] is to confirm facts, data and representations involved in a commercial transaction in order to determine the value, price and risk of such transactions, including the risk of future litigation.[126]

The focus of this business due diligence is on the direct risk to the business and management of the process, which is usually a one-off process.

However, human rights due diligence brings in an international human rights law approach of an external, 'objective' standard of conduct to take reasonable precautions to prevent, or to respond to, certain types of harm specified by the rule in question.[127] It is thus a different focus and is also an on-going expectation. This is clear from the definition of human rights due diligence by the Office of the High Commissioner of Human Rights:

> [Human rights due diligence is] a measure of prudence, activity, or assiduity, as is properly to be expected from, and ordinarily exercised by, a reasonable and prudent [person or enterprise] under the particular circumstances; not measured by any absolute standard, but depending on the relative facts of the special case. In the context of the Guiding Principles, human rights due diligence comprises an ongoing management process that a reasonable and prudent enterprise needs to undertake, in light of its circumstances (including sector, operating context, size and similar factors) to meet its responsibility to respect human rights.[128]

Thus human rights due diligence process 'can be incorporated within other processes such as risk assessments or environmental and social impact assessments, they should include all internationally recognized human rights as a reference point'.[129] Therefore, to comply with the UNGPs a company is meant to consider the human rights impacts to stakeholders other than shareholders, such as local communities, wherever they operate and to do so on an ongoing basis. This notion of 'prudence' in the UNGPs is not that far from the idea of the duty of care of a diligent businessperson found in the laws of all EU Member States, as seen above.

Interestingly, under the Danish Financial Statement Act companies must expressly state in their reports what measures they are taking to respect human rights and to reduce their impact on the climate, and the description of a company's policies must include a description of 'due diligence processes implemented'.[130] This section specifically uses the term 'due diligence', though it does not define it, yet the Danish government has noted that this concept of due diligence exists in the OECD Guidelines for Multinational Enterprises and the UNGPs. Similarly, the academic report on the German

[126]Olga Martin-Ortega, 'Human Rights Due Diligence for Corporations: From Voluntary Standards to Hard Law at Last?' (2013) 31 *Netherlands Quarterly of Human Rights* 44, at 51.
[127]See Bonnitcha and McCorquodale (n 9).
[128]The Office of the UN High Commissioner on Human Rights (OHCHR), 'The Corporate Responsibility to Respect: An Interpretive Guide' (2012).
[129]Commentary to Guiding Principle 18.
[130]Denmark Financial Statements Act 2001, section 99a.

National Baseline Assessment for implementing the UNGPs proposes to examine whether and how due diligence obligations could be better integrated into the supervisory role of the board of directors, given the important monitoring role the latter could play in ensuring corporate respect for human rights.[131]

As indicated above, the board of directors would be expected to have both oversight and advice in relation to these matters. Indeed, in relation to the creation of a policy of human rights due diligence the UNGPs make clear that it should be 'approved at the most senior level of the business enterprise'.[132] This is confirmed by the OECD in its Due Diligence Guidance for Responsible Business Conduct:

> Boards will generally be involved in approving an enterprise's [Responsible Business Conduct (RBC)] policies. They may also be involved in taking decisions about a business strategy which may have implications for RBC. Additionally, they may intervene in instances where the RBC policies are not being implemented and request management to take action. It can be useful to appoint board member(s) with expertise on and responsibility for RBC issues. In this respect the G20/OECD Principles of Corporate Governance recognised that *an important responsibility of the board of public enterprises is to oversee the risk management system* and systems designed to ensure that the corporation obeys applicable laws, including tax, competition, labour, environmental, equal opportunity, anticorruption, and health and safety laws (OECD, 2015a, Ch.VI). Management, on the other hand, will be responsible for developing a strategy to ensure the RBC policy is implemented. While the role of boards and management is distinct, in practice high-level management personnel may sit on enterprise boards and thus play a dual role.[133]

This is a powerful statement by an authoritative body as to why there is a responsibility on directors in the area of human rights. Indeed, the European Commission has stated that boards have a 'vital part to play in the development of responsible companies'.[134]

It is feasible to conclude that shareholders may, in time, bring claims against companies for not taking human rights issues sufficiently into account in their strategies and operations, such as by failing to adopt and implement human rights due diligence processes. It was seen that there are now cases successfully brought against companies in the EU for human rights impacts. However, if there is legislation on this area it would increase

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[131]See Deutsches Institut für Menschenrechte, *National Baseline Assessment: Umsetzung der UN-Leitprinzipien für Wirtschaft und Menschenrechte* (2015) 15; considering as an example the role of due diligence obligations in the context of vicarious corporate liability laid down in the German Civil Code, Article 831, see <www.institut-fuer-menschenrechte.de/publikationen/show/national-baseline-assessment-umsetzung-der-un-leitprinzipien-fuer-wirtschaft-und-menschenrechte/>.

[132]Guiding Principle 16.

[133]OECD, *Due Diligence Guidance for Responsible Business Conduct* (2018) 59 (emphasis added).

[134]European Commission, *Green Paper – The EU Corporate Governance Framework* (2011) 164, at 5.

the risks to the company and the directors. In the meantime, directors would seem to be wise to establish proper risk management systems which enable them to identify, monitor and address risks, including reputational and operational risks in this area.

9. Personal liability of directors

As seen above, directors' duties under corporate law are owed to the company. Where those duties are breached, the remedy sought is generally the return of any profits made by the director to the company, or for other consequential loss, or an injunction against the director/s and termination of contracts. However, a claim by the company (or shareholders on its behalf) is not the only means through which a director may be held personally liable for their conduct in office. In some situations, a director may face criminal or regulatory enforcement (potentially resulting in fines or imprisonment depending on the gravity and nature of any offence) and regulatory authorities may prevent the director acting as a director again.[135] There are also rare circumstances where persons affected by a company's conduct could bring civil claims against the company's directors, usually jointly with the company as a co-defendant. These additional routes to director liability are worth noting, as they may inform the framework of any draft EU human rights and environment due diligence law proposed by the European Commission.

Personal liability for the director can arise in circumstances where it can be shown that a company report caused specific damage, and that this damage was the responsibility not of the company but of the director themselves.[136] For example, under UK law a director is liable to compensate the company for any loss resulting from an untrue or misleading report, provided they knew the statement was untrue or misleading or was reckless as to its veracity.[137] Similarly, a failure to publish statutorily requirement information also presents a risk for directors. For example, under the French Duty of Vigilance Act, if the annual management report does not include the required vigilance plan, any interested person may ask the court in the context of interim/emergency proceedings to order the company's board of directors or its executive board to communicate the required information. When the injunction is granted, the fine and costs of proceedings (and possibly any damage caused) shall be

[135] See, for example, Germany's Administrative Offences Act (*Ordnungswidrigkeitsgesetz*) 1986, Article 130, Ireland's 2017 Regulations implementing the EU Directive on Non-Financial Reporting and the Irish Human Rights and Equality Commission Act 2014, section 8, and UK Companies Act, section 178.
[136] See, for example, France Commercial Code, Article L. 225-102.-1, VI and Italy Civil Code, Article 2392.
[137] See section 463(1) – (3) of the UK Companies Act. Note that in the case of an omission a director can be liable if they knew the omission was a dishonest concealment of a material fact. A director can also be personally liable in relation to tax evasion under the UK Finance Act 2020.

borne by the directors or members of the executive board, individually or severally.[138]

In addition, directors can be subject to a range of specific statutory duties and liabilities, such as under health and safety, labour and security regulations, and under criminal law. For example, under the Spanish Environmental Liability Act,[139] there is an obligation on certain companies to undertake an environmental impact assessment. This includes a provision that where the harm is caused by a subsidiary of a parent company under the instructions of such parent company or using the subsidiary fraudulently to limit liability, the parent company will be vicariously liable.[140] This legislation expands corporate liability to managers and directors whose conduct has been determinant of the responsibility of the company, so that they will be responsible for obligations and liabilities. Therefore, directors or managers of a corporation whose conduct has been a driving factor in the damage caused, as well as liquidators in the case of bankruptcy, can be held personally liable.[141]

These particular types of provisions in legislation can result in a director personally facing criminal sanction (e.g. imprisonment and/or a fine),[142] compensation orders,[143] civil claims[144] or disqualification[145] in the event of non-compliance. As seen in the Spanish example above, the director's liability is often derivative of a company's failure to comply with applicable laws and obligations, though, as in the instances of disqualification from being a director, it is usually due to a direct and personal action by the director. The aim in each instance is to put personal pressure on directors to ensure that there are actual changes in a company's approach and not just considering that a fine or other costs of not undertaking human rights due diligence as being merely financial costs to the business without due regard to the victims.

In the context of financial services regulation, the senior managers' regime implemented in the UK in 2016 requires that financial institutions and insurance companies map responsibilities and identify the individuals responsible

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[138]France Commercial Code, Article L. 225-102.-1, VI. Thus the French legislature has taken the position that some limited liability can be imposed on directors under this legislation.

[139]Law 26/2007, of 23 November 2007, on Environmental Liability. This transposes the European Directive 2004/35/EC, of the European Parliament and of the Council, of April 21, on environmental responsibility in relation to the prevention and repair of environmental damage.

[140]ibid, Article 10.

[141]Ibid, Article 13.

[142]For example, UK Health and Safety at Work etc. Act 1974, section 37 (1), which provides that where an offence against worker safety etc., is committed by a company, a director will be guilty of the same offence provided it can be proved the offence was 'committed with the consent or connivance of' the director, or was otherwise proved 'to have been attributable to any neglect on the part of' that director: see *R v Rollco Screw and Rivet Co Ltd* [1999] 2 Cr App Rep (S) 436, CA.

[143]For example, sections 130–33 Powers of Criminal Courts (Sentencing) Act 2000, sections 130–32.

[144]For example, UK Financial Services and Markets Act 2000, section 90(1) concerning false or misleading statements in listing particulars or a prospectus.

[145]For example, UK National Minimum Wage Act 1998 <www.gov.uk/government/news/director-banned-after-failing-to-pay-minimum-wage-to-farm-labourers>.

for key areas of governance, compliance and operations to increase individual accountability. As a consequence, senior managers can now be held accountable for the misconduct of others falling within their area of responsibility but only if the senior manager did not take such steps as a person in the senior manager's position could reasonably be expected to take to avoid the misconduct occurring (or continuing).[146] In addition, under the UK Bribery Act if a bribery offence is committed by a company then any senior officer of that company is guilty of the same offence if they consent to or connive in the commission of the offence, provided that, if the offence is committed outside the UK, they have a close connection to the UK.[147]

Under tort law in a few Member States it is possible for victims to bring a claim against directors personally. For example, under Italian law directors are jointly and severally liable (i.e. each director individually and as a group of directors) toward the company, the shareholders, and third parties in general for damages suffered by each of them as a direct result of the directors' negligence in fulfilling their fiduciary duties according to law, articles of incorporation and by-laws.[148] It is also recognised in common law jurisdictions that a director can be jointly liable for torts committed by a company where that director authorised, directed or procured those torts.[149] In each instance, victims have to prove the causal link between the violation of an obligation of the director and the damage suffered. This is generally difficult to prove.

10. Going forward

The current position is that there is no legislation in the EU and the UK which clearly creates a liability for directors who do not take action in relation to human rights and environmental risks, though there are a number of indications in case law which show the possibility of director's liability in limited situations. However, the proposal for EU-wide legislation addressing the scope of directors' duties, particularly in the context of human rights and the environment, recognises that there are risks if the current position does not change, with the European Commission noting:

[146] UK Financial Services and Markets Act 2016, section 66A(5).

[147] UK Bribery Act 2010, section 14. Note, though, that section 14 only applies where the company commits an offence with a *mens rea* component; i.e. the general bribery offence in section 1 and the offence of bribing a foreign public official in section 6. It does not apply where the company commits an offence under section 7 ('failure to prevent bribery') which is strict liability.

[148] Italy Civil Code, Article 2392. In particular, directors are liable if they carry out detrimental acts, or if, being aware of detrimental acts, they do not act to prevent their occurrence or to eliminate or reduce their harmful effects or if they fail to supervise the general management. The responsibility of the directors towards the shareholders and third parties, means that the shareholders and third parties can ask the administrators for compensation for damages only in the event that the performance of an unlawful act by the directors in the exercise of their office has caused direct damage to the assets of the individual shareholder or of the single third party.

[149] See *Rainham Chemical Works Limited v Belvedere Fish Guano Co Limited* [1921] 2 AC 465.

> [P]ressure [on directors] to focus on short-term financial performance reduces companies' ability to integrate sustainability considerations adequately into business strategies and decisions. This has two aspects: on the one hand, companies do not properly identify and address climate change and other environmental, social and human rights (including workers' rights, child labour etc.) risks and impacts in their operations and supply chains .... On the other hand, companies fail to integrate potential new opportunities either for investment or for building resilience.[150]

This statement highlights the direct risks to companies of failing to identify and respond to human rights and environment risks, particularly given the growing probability of new EU legislation in this area.

As noted above, all directors are responsible for risk management, which clearly links with their duties to act in the best interests of the company and to exercise reasonable care, skill and diligence. If human rights and environmental due diligence were to become a mandatory obligation for companies – with sufficiently serious consequences in terms of sanctions in the event of breach – the existing obligations on directors to exercise risk management oversight could serve effectively to incentivise directors to respond proactively to manage the company's potential liability under the law. This is no different from any business activity which could result in significant legal or operational risks, such as suspended mining activities because of community protests. Failure to manage such risks could put directors in breach of their duties.

However, there is also an argument that the introduction of specific obligations on directors, alongside their directors' duties (perhaps similar to the senior managers' regime in the UK's financial services sector) would result in directors monitoring more proactively how companies identify and manage their human rights and environmental impacts. The developments in the expansion of directors' duties, and broad consensus that directors should consider stakeholders beyond solely the company's shareholders, are significant. It could be seen as means to press directors to ensure that companies do not adversely impact human rights.[151]

The German National Baseline Assessment for implementing the UNGPs proposed to examine whether and how due diligence obligations could be better integrated into the supervisory role of the board of directors, given the important monitoring role the latter could play in ensuring corporate

[150] EC, Sustainable Corporate Governance (n 3).

[151] Changes in company law to reflect the need for directors to act in accordance with a social purpose of companies, to extend directors' accountability and to secure sustainability have been canvassed: see Beate Sjåfjell, 'How Company Law has Failed Human Rights – And What To Do About It' (2020) 5 *Business and Human Rights Journal* 179. There is also some criticism of the stakeholder approach: see Lucian Bebchuk and Roberto Tallarita, 'The Illusory Promise of Stakeholder Governance' (2020) 106 *Cornell Law Review* 91.

respect for human rights,[152] as the board of directors should exercise its supervisory functions by the imposition of reporting duties on the company's management.[153] The Swiss government's counter-proposal to the Business and Human Rights Initiative includes an oversight role to the board of directors:

> The board of directors takes measures to ensure that the company complies with the provisions for the protection of human rights and the environment relevant to its areas of activity, including abroad. It identifies potential and actual impacts of the business activities on human rights and the environment and assesses these risks. Taking into account the company's ability to exert influence, it takes effective measures to minimize the identified risks concerning human rights and the environment as well as to ensure effective remedy for violations. It monitors the effectiveness of the measures adopted and reports on them. Impacts of business activities of controlled companies or due to business relationships with a third party are also subject to this due diligence.[154]

This counter-proposal is not yet legislation but might be one way to consider these issues. Yet it is rather vague in terms of clarifying what risk management measures need to be taken by the board of directors. Therefore, a closer link between the director's personal oversight obligation and the company's primary compliance obligation may place more pressure on a director and senior management to act. The UK Bribery Act is one example of a law which takes this approach. Where a company commits a strict liability bribery offence, it is a defence for the company to show that it had adequate anti-bribery procedures in place at the time the bribery occurred. Thus active oversight by directors and senior management is inherent to an effective compliance programme, and thus the availability of the defence.

The Swiss counter-proposal is consistent with a range of legislation across the EU Member States in which there are some responsibilities on directors to ensure that a company complies with its legal obligations. Thus a specific obligation placed on both directors and senior managers to ensure the performance of human rights and environmental due diligence by the company could be part of the new EU legislation, where a failure of a director to do so could result in a breach of their oversight obligations. A regulatory authority would need to be in place to ensure effective compliance.[155]

[152]Deutsches Institut für Menschenrechte, *National Baseline Assessment: Umsetzung der UN-Leitprinzipien für Wirtschaft und Menschenrechte* (2015) 15.

[153]Article 90 German Commercial Code.

[154]Swiss Counter-Proposal, unofficial English translation: <www.bhrinlaw.org/180508-swiss-parliament-counter-proposal_unofficial_en-translation_updated.pdf>.

[155]Any such legislation would probably need to be accompanied and supported by other reforms in both the public and the private sector. For example, human rights issues could feature more prominently in stock exchange listing requirements as well as public procurement conditions, and more robust human rights requirements could be incorporated into industry-wide agreements adopted by finance institutions. Such reforms are the subject of regular discussions involving civil society, governments and businesses (for example at multi-stakeholder events such as the annual UN Forum on Business and Human Rights) but are outside the scope of this article.

However, there are two important limitations on these developments: the consequence on directors; and the remedies for victims. First, with the potential increase in the array of potential risks which directors have to take into account as part of their duties, it might become more difficult for individuals to agree to become directors of companies due to the potential liabilities involved. This may result in less experienced individuals accepting director appointments, as better qualified candidates perceive the role to be less attractive in light of the enhanced personal risks, though the authors are not aware of any study confirming such a phenomenon following the introduction of more stringent regulation in other areas. A related concern, that of directors feeling more constrained in their decision making, was referred to in a draft EU Directive that '[it] is important to ensure that directors are not dissuaded from exercising reasonable business judgment or taking reasonable commercial risks'.[156] This dissuasion might also be relevant if existing companies include a specific social purpose within their purposes.

Second, the developments in extending the duties and statutory obligations of directors and expanding the types of risk for which they should be taking action, does not change the position of the victims of a human rights impact arising from the company's activities. As stated above, the director owes a duty towards the company. Even if the company is insolvent and the duty is owed to the creditors, it is the company (through its receivers or administrators) which can bring the action. In the case of a derivative action brought by shareholders for breach of duty, the claim is brought by the shareholders (on behalf of the company) given the consequential impact to those shareholders arising from the directors' breaches. By contrast, where a director commits a criminal or regulatory offence, any resulting enforcement action against that individual will be brought by the competent regulator or prosecutorial authority. In none of these circumstances can a victim bring an action against directors for their decisions (or other relevant acts or omissions) which led to the victim's human rights being abused by the company. The cases brought by such victims to date seeking remedies, as set out above, have been against companies and not against the directors.

While the possibility of tort claims against a company's directors is referred to above, the only instances where there has been such a claim against directors personally is where there is a crime (when there is no automatic remedy to the victims) or where there is a statutory breach by the company (e.g. of minimum wage laws, per the English *Antuzis* case, cited above) which can be linked with the director's duty because of the director's high degree of personal involvement in procuring that statutory breach. However, it is less

[156] Proposed EU Directive on preventive restructuring frameworks, on discharge of debt and disqualifications, and on measures to increase the efficiency of procedures concerning restructuring, insolvency and discharge of debt, and amending Directive (EU) 2017/1132, para 70.

likely that directors of large companies will be knowingly complicit in this sort of misconduct, though in Belgian law, it is a crime to breach the obligation to give a true image of the company in the annual report if the victim can prove the causal link[157] and under Italian law, it is possible to join the director in a claim against the company.[158]

Thus the situation is one where, even if it were possible to expand and develop some regulations about the duties and statutory obligations of directors in relation to human rights, including human rights due diligence, the end result would generally not be a remedy direct to the victims. It would require new legislation and a significant change in company law in the EU Member States for this to occur, with perhaps some risk of the directors' duties becoming too vague to enforce effectively.

11. Conclusions

Directors' duties are critically important to effective corporate governance and the scope of these duties has been expanding. After a comparative examination across EU Member States regarding how directors' duties are formulated and understood in different jurisdictions, it is evident that directors' duties are largely owed only to the company and there are limited circumstances where directors are personally liable. There is, though, some scope to broaden the best interests of the company so that directors can include consideration of matters such as human rights and the environment. These developments do not generally provide for a means for a victim of a human rights impact caused by a company (acting on a decision of its directors) to bring a claim against those directors. At best a victim may be able to bring an action for damage to the company (such as in tort) or, in the rare case that the company is subject to a criminal conviction, receive compensation, not least as a company will probably have greater resources than its directors.

Therefore, the proposal by the European Commission to include directors' duties as part of legislation on human rights and environmental due diligence is important, even if there may be resistance from some jurisdictions to whatever is the final proposal.[159] Making directors personally liable to the individuals whose human rights were infringed by the activities of a company may require broader changes in the nature or scope of the existing directors' duties across EU Member States. Any changes to directors' duties in this area could be along the lines adopted by the King Committee on Corporate Governance in South Africa:

[157] Belgium Company Code, Article 128 *jo.* 96.

[158] Italy, L.D. no. 231/2001.

[159] It is, though, relevant that every EU Member State and the UK implemented in full the EU Directive on Non-Financial Reporting, as set out above.

> Directors duties include: (i) ensuring that the company acts as, and is seen to be, a responsible corporate citizen; (ii) cultivating and promoting an ethical corporate culture; (iii) considering sustainability as a business opportunity; (iv) ensuring the integrity of financial reporting; and (v) ensuring that the company implements an effective compliance framework and processes.[160]

The authors consider that there is some justification for legislation which provides that directors and senior managers can be held accountable for not taking reasonable steps to ensure that human rights and environmental due diligence processes were undertaken within the company. For example, under section 172 of the UK Companies Act, the directors would have to ensure – as part of their duties of monitoring the activities of the company – that the company's human rights and environmental due diligence process occurred.

Accordingly, directors would be well advised to require companies to adopt management systems which include human rights due diligence, including in relation to environmental and possibly climate change impacts, now and act in advance of any EU legislation. Such due diligence should be sufficient to ensure that the directors are aware of the company's most severe potential human rights impacts arising from its activities and business relationships, and that they are well-informed regarding the effectiveness of the steps being taken by the company to mitigate those impacts. This should reduce both the impacts and the possibility of claims brought for lack of consideration by directors of these risks. As the *Caremark Case* made clear:

> [I]t would … be a mistake to conclude that … corporate boards may satisfy their obligation to be reasonably informed concerning the corporation, without assuring themselves that information and reporting systems exist in the organization that are reasonably designed to provide to senior management and to the board itself timely, accurate information sufficient to allow management and the board, each within its scope, to reach informed judgments concerning both the corporation's compliance with the law and its business performance.[161]

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[160]See <www.iodsa.co.za/page/kingIII>. Many of these principles are now embodied in the South African Companies Act 2008.

[161]*Caremark* (n 45) at para 970.

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