From Corporate Social Responsibility to Sustainable Corporate Governance: The New CSRD

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INTRODUCTION

Corporate governance outlines the processes and methods to direct and control a business. In the past, maximizing shareholder value was the main goal of corporate governance, but the development of a global society demanded enterprises to consider other stakeholders' interests, embracing the concept of Corporate Social Responsibility (CSR). This change is underpinned by the idea that corporations can no longer act as isolated economic entities operating in detachment from broader society[1].

According to European Law, corporate social responsibility is defined as "a concept whereby companies integrate social and environmental concerns in their business operations and in their interaction with their stakeholders on a voluntary basis."[2] In this sense, EU legislation refers to CSR as a company's responsibility to operate in a manner that benefits society as a whole, in addition to its financial stakeholders. It includes concerns like reducing environmental impact, treating employees fairly, and respecting human rights.

It is important to assert that voluntariness was put as a key component of the definition of CSR. This feature is also present in other EU documents, such as the Green Paper[3] and the Commission's Communication of 2 July 2002, in which the Commission recognizes the voluntary nature of CSR, stating that it "is behavior by businesses over and above legal requirements, voluntarily adopted because businesses deem it to be in their long-term interest."[4] In recent years, however, the emphasis is switching from a voluntary approach to a mandatory one, leading CSR to Sustainable Corporate Governance (SCG).

A brief analysis of the CSRD and its impact on the NFRD, the SFDR, and the EU Taxonomy

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[1] Kumari, Pinki, CSR: From Voluntary to Mandatory (January 10, 2013). Available at: https://ssrn.com/abstract=2779341 [accessed 20 February 2023]

[2] Communication from the Commission to the European Parliament, the Council and the European Economic and Social Committee of March 2006. 22 March 2006, COM(2006) 136 final, available at: https://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2006:0136:FIN:en:PDF [accessed 20 February 2023]

[3] "Corporate social responsibility is essentially a concept whereby companies decide voluntarily to contribute to a better society and a cleaner environment." GREEN PAPER Promoting a European framework for Corporate Social Responsibility, 18 July 2001, COM(2001) 366 final, available at: https://www.europarl.europa.eu/meetdocs/committees/deve/20020122/com(2001)366_en.pdf [accessed 20 February 2023]

[4] COMMUNICATION FROM THE COMMISSION concerning Corporate Social Responsibility: A business contribution to Sustainable Development. 07 July 2002 COM(2002) 347 final, available at: https://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2002:0347:FIN:en:PDF [accessed 20 February 2023]

While CSR was initially voluntary, the Non-Financial Reporting Directive (NFRD), published in 2014, created reporting and transparency obligations on sustainability matters for large-public interest European companies, requiring them to disclose information about environmental, social, and governmental (ESG) issues in their non-financial statements[5]. In 2022, the new Corporate Sustainability Reporting Directive (CSRD) went beyond and extended the scope of companies subject to mandatory sustainability reporting obligations regarding the previous NFRD[6].

The new EU directive on Corporate Sustainable Responsibility requires all large and all listed companies to perform due diligence and report on their environmental and social impact in their value chain, as well as promotes the standardization of reported information. In other words, it adds the corporate duty to integrate "sustainability into corporate governance and management systems, and framing business decisions in terms of human rights, climate and environmental impact, as well as in terms of the company's resilience in the longer term."[7] In addition, the Directive addresses the issue that the NFRD's framework created, which was a variety of conflicting reported data without a standard against which to compare it.

Besides, the CSRD supports the Sustainable Finance Disclosure Regulation (SFDR), which applies to financial market participants and financial advisers. According to the SFDR, these undertakings must, among other things, make a statement on their due diligence procedures regarding the principal adverse impacts of their investment choices on sustainability issues on a comply-or-explain basis. The publication of such a statement is required for businesses with more than 500 employees, and the Commission has the authority to create regulatory technical standards on the sustainability indicators to the various forms of negative impacts[8].

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[5] 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. 15 November 2014. available at: https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32014L0095&from=EN [accessed 28 February 2023]

[6] DIRECTIVE (EU) 2022/2464 OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL of 14 December 2022 amending Regulation (EU) No 537/2014, Directive 2004/109/EC, Directive 2006/43/EC and Directive 2013/34/EU, as regards corporate sustainability reporting. 16 December 2022. available at: https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A32022L2464 [accessed 28 February 2023]

[7] Proposal for a DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL on Corporate Sustainability Due Diligence and amending Directive (EU) 2019/1937. 23 February 2022 COM(2022) 71 final, p. 1. available at: https://ec.europa.eu/transparency/documents-register/detail?ref=COM(2022)71&lang=en [accessed 28 February 2023]

[8] Proposal for a DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL on Corporate Sustainability Due Diligence and amending Directive (EU) 2019/1937. 23 February 2022 COM(2022) 71 final, p. 5. available at: https://ec.europa.eu/transparency/documents-register/detail?ref=COM(2022)71&lang=en [accessed 28 February 2023]

At the same time, the new Directive also complements the EU Taxonomy Regulation[9], which categorizes environmentally friendly investments in economic activities that fulfill a minimum social safeguard, simplifying investment decisions and combating "greenwashing." The Taxonomy Regulation can be used to help businesses acquire sustainable funding by establishing a consistent vocabulary for sustainable economic activity for investment reasons[10]. In this sense, the CSRD completes the Taxonomy Regulation since it makes it easier for investors to direct money toward ethical and sustainable businesses through the reported information.

Regarding compliance, the new EU directive on Corporate Sustainable Responsibility determines that measures related to public enforcement of due diligence must be proportionate. In this sense, if the company's compliance with this Directive is under investigation by public authorities, they must first give the company a reasonable amount of time to take corrective measures[11]. Additionally, the CSRD leaves it to the Member States, which have by 6 July 2024 to transpose its determinations into national law, to ensure a proportionate enforcement process[12].

In short, the Corporate Sustainability Reporting Directive sets up a framework for enabling Sustainable Corporate Governance. Given that companies' behavior is key to success in the Union's transition to a climate-neutral and green economy[13] and that voluntary

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[9] REGULATION (EU) 2020/852 OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL of 18 June 2020 on the establishment of a framework to facilitate sustainable investment, and amending Regulation (EU) 2019/2088. 22 June 2020. available at: https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32020R0852&from=EN [accessed 28 February 2023]

[10] Proposal for a DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL on Corporate Sustainability Due Diligence and amending Directive (EU) 2019/1937. 23 February 2022 COM(2022) 71 final, p. 5. available at: https://ec.europa.eu/transparency/documents-register/detail?ref=COM(2022)71&lang=en [accessed 28 February 2023]

[11] Proposal for a DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL on Corporate Sustainability Due Diligence and amending Directive (EU) 2019/1937. 23 February 2022 COM(2022) 71 final, p. 17. available at: https://ec.europa.eu/transparency/documents-register/detail?ref=COM(2022)71&lang=en [accessed 28 February 2023]

[12] See Article 28a, (20) 2 of the DIRECTIVE (EU) 2022/2464 OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL of 14 December 2022 amending Regulation (EU) No 537/2014, Directive 2004/109/EC, Directive 2006/43/EC and Directive 2013/34/EU, as regards corporate sustainability reporting. 16 December 2022: 'Without prejudice to their civil liability regimes, Member States shall provide for effective, proportionate and dissuasive sanctions in respect of statutory auditors and audit firms, where statutory audits or assurance of sustainability reporting are not carried out in conformity with the provisions adopted in the implementation of this Directive, and, where applicable, with Regulation (EU) No 537/2014'. available at: https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A32022L2464 [accessed 28 February 2023]

[13] Regulation (EU) 2021/1119 of the European Parliament and of the Council of 30 June 2021 establishing the framework for achieving climate neutrality and amending Regulations (EC) No 401/2009 and (EU) 2018/1999 ('European Climate Law'), which also includes a binding target to cut domestic net greenhouse gas emissions by at least 55% compared to 1990 levels by 2030. 09 July 2021 available at: https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A32021R1119 [accessed 03 March 2023]

action did not deliver the expected results across market sectors[14], the CSRD creates legal certainty for businesses and stakeholders as regards expected behavior and liability.

CONCLUSION

In line with the Green Deal and the Paris Agreement, the EU aims to achieve a net-zero emission of greenhouse gases by 2050 while shielding Union inhabitants' health and well-being from environmental hazards and adverse effects. Yet, these goals cannot be detached from a modern and competitive economy; and there is already an increased awareness from investors of the risks and opportunities resulting from sustainability issues.

Considering the above, Sustainable Corporate Governance takes a step further with the new Corporate Sustainability Reporting Directive by emphasizing a company's responsibility to operate sustainably and to use European Sustainability Reporting Standards[15]. By putting sustainability reporting on an equal basis with financial reporting, the CSRD becomes a promising tool for the EU to ensure that its market business model and strategy are compatible with the transition to a sustainable economy.

While some companies may view these requirements as burdensome, many recognize the benefits of adopting sustainable practices. SCG can help companies reduce risk, build stakeholder trust, and even improve financial performance. In fact, a Harvard Business School study[16] found that companies with strong sustainability practices outperformed their peers over the long term in terms of stock market performance and accounting performance.

In conclusion, the focus on corporate governance has evolved over the years from a narrow focus on shareholder value to a broader focus on CSR and now on SCG. While the shift from voluntary to mandatory adoption of these principles may be challenging for some companies, there are many benefits to adopting sustainable practices. Ultimately, companies that embrace SCG are likely to be more successful in the long run, both financially and in terms of their impact on society and the environment.

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[15] Guide to the Corporate Sustainability Reporting Directive: Preparing for the CSRS. January 2023. Mazars. available at: https://www.mazars.com/Home/Services/Sustainability/Sustainability-regulations/Preparing-for-the-CSRD/Guide-to-the-CSRD [accessed 28 February 2023]

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