

# Corporate Climate Responsibility – The Rise of a New Governance Issue

Given the absence of a comprehensive regulatory framework, international recommendations and best practices on corporate responsibility in the area of climate change are emerging. Due to their financial materiality, climate change risks have recently gained widespread recognition by international organizations and financial regulators. Accordingly, sound corporate governance requires companies to have regard to climate change issues. The authors propose the term ‘Corporate Climate Responsibility’ to frame various trends in legal doctrine and market developments.

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## I. Introduction

- 1 Human rights and environmental issues have often been approached from the angle of Corporate Social and Environmental Responsibility (CSR). This is a concept according to which, in essence, the corporate purpose extends beyond creating shareholder value by encompassing social and environmental issues. From a corporate law perspective, the initial question in this context is what the role or purpose of corporations in society is: whether to only focus on shareholder wealth, or whether to also have regard to other stakeholders' interests, including the interest in a healthy environment or, more drastically, a livable planet for future generations.
- 2 Despite the widely acknowledged need for substantial measures to prevent the most disastrous effects of climate change, binding "hard law" obligations on corporations to reduce their greenhouse gas (GHG) emissions are scarce, sector specific and arguably non-efficient, considering the still rising levels of global GHG emissions.<sup>1</sup> While climate change has typically been viewed as an issue to be addressed primarily at the intergovernmental level, more recently, a new focus on the role of the private sector in achieving global GHG emissions reductions has emerged.
- 3 Corporate responsibility in the climate change context increasingly attracts the attention of scholars, policymakers and society. This begs the question how to contextualize this new legal issue within the existing legal landscape, whilst also having regard to current market developments in the area. To this end, the authors propose the term Corporate Climate Responsibility (CCR) as a means to capture and contextualize various climate change related trends in the legal sphere as well as changing market practices.
- 4 With a particular focus on environmental protection, the first part of the article (II) analyzes the evolution from corporate governance to CSR, including the revisiting of the corporate purpose, the broadened foundations of CSR, and the trend towards the "hardening" of soft law. Sketching the contours of CCR, the second part (III) outlines the rationale for introducing CCR by formulating three hypotheses and then discusses the main drivers of the new focus on climate change in the corporate world,

1 See United Nations Environment Programme (UNEP), *Emissions Gap Report 2020: Executive Summary*, 2020 (highlighting that the COVID-19 crisis "offers only a short-term reduction and will not contribute significantly to emissions reductions by 2030 unless countries pursue an economic recovery that incorporates strong decarbonization").

the business response to the regulatory framework as well as key elements and the legal quality of CCR.<sup>2</sup>

## II. From Corporate Governance to Corporate Social and Environmental Responsibility

### 1. Increased Importance of Governance

The term "governance" can be traced back to the Greek word "kybernetes", the "steersman", and the Latin word "gubernator". These historical roots lead to the English notion "governor" and therefore relate to aspects of steering or governing behavior.<sup>3</sup> Already in ancient Greece, entrepreneurs and traders had certain responsibilities towards their community.

The governance discussion first started out in the private domain under the well-known concept of corporate governance. Companies are expected to implement structures that allow them to comply with the given allocation of duties and responsibilities. During the last 20 years, many corporate governance codes and guidelines have been developed. Nonetheless, the term corporate governance is only rarely reflected in legal statutes of national legislators. But the concept has expanded to further regulatory structures, including the public sector, both at the national and the international level.<sup>4</sup>

Today, companies are considered (at least in academia) not only as economic, but also as social actors. Consequently, the term corporate governance has been broadened and further developed into the concept of CSR.<sup>5</sup> Describing CSR, the European Commission originally referred to a "concept whereby companies integrate social and environmental concerns in their business operations and in their interaction with their stakeholders on a voluntary basis".<sup>6</sup> Such framing of CSR as a *voluntary*

2 The authors fully acknowledge the multifaceted complexity of the issue discussed herein. A comprehensive analysis of all relevant developments and legal aspects goes beyond the scope of this article. For instance, the authors do not discuss the role of carbon pricing mechanisms such as emission trading systems. It is also noted that a comprehensive concept of CCR would likely include further aspects including, for instance, board composition, remuneration, target setting, etc. In that sense, this article undertakes a first "sketch" of CCR.

3 ROLF H. WEBER, *Shaping Internet Governance: Regulatory Challenges*, Zurich 2010, p. 2.

4 WEBER (fn. 3), p. 3.

5 CHRISTINE KAUFMANN, *From Profit to People and Planet: Rethinking the Purpose of the Company*, in: Weber/Stoffel/Chenau/Sethe (eds.), *Aktuelle Herausforderungen des Gesellschafts- und Finanzmarktrechts*, Zurich 2017, p. 6. Regarding the history of CSR see KRISTA NADAKAVUKAREN SCHEFER, *Social Power, Social Responsibility, and Corporations: from CSR to Business and Human Rights*, ZSR 139/2020 II, p. 24.

6 European Commission, *Green Paper: Promoting a European framework for Corporate Social Responsibility (COM [2001] 366 final)*, p. 6.

endeavour received criticism due to its tendency to prioritize shareholder wealth over environmental and social interests.<sup>7</sup> Accordingly, the term CSR was further developed and refined to encompassing companies' responsibility for their impacts on society and the environment. To fully meet their CSR, companies "should have in place a process to integrate social, environmental, ethical, human rights and consumer concerns into their business operations and core strategy in close collaboration with their stakeholders".<sup>8</sup> As a consequence, governance gained wider importance in the corporate law field.<sup>9</sup>

8 CSR compliance attempts to implement and supervise mechanisms which have the objective to achieve values and reputation through behavioral processes. In particular, businesses are expected to observe social and environmental objectives, demonstrate a high level of integrity and transparency, and thereby enhance social welfare.<sup>10</sup> The word "responsibility" is linked to the conduct of the company in the market, encompassing its relationship to employees and customers as well as its commitments to applying ethical behavior.<sup>11</sup> Relevant aspects are respect, integrity, communication, and excellence.<sup>12</sup>

## 2. Revisiting the Purpose of the Company: Respect for the Environment?

9 Traditionally, the purpose of the company is expressed in its articles of association and, therefore, determined by the shareholders. Over the last two decades, often challenging Friedman's statement that the only, or at least primary, purpose of the company consists in increasing its profits<sup>13</sup>, a myriad of papers have discussed

the potential purposes of a corporation. While it is increasingly acknowledged that a company is "a moral organism with social and ethical responsibilities",<sup>14</sup> some scholars argue that the maximization of shareholder value as the sole purpose of a corporation rests on faulty assumptions and is "to a great extent incorrect as a matter of law".<sup>15</sup> The wide range of stakeholders whose interests ought to be considered includes employees, customers, and suppliers but also communities and other stakeholder groups, for example civil society, and – critical in the climate change context – the environment.<sup>16</sup> Accordingly, CSR encompasses both social and environmental responsibility.<sup>17</sup>

More consideration to environmental concerns is also reflected by the "triple bottom line", a concept introduced in the nineties, according to which companies should realize three objectives: (i) profit optimization in the interest of the shareholders, (ii) socially and ethically responsible behavior in the interest of the employees and civil society, as well as (iii) resources-saving in the interest of environment protection.<sup>18</sup> Partly, self-regulatory guidelines have taken up this idea. For example, in its current version, the German Corporate Governance Codex states that social and environmental factors have an influence on entrepreneurial success.<sup>19</sup>

A new vision of corporations calls for a radical reform of the concept of corporations, their business objective, roles and responsibilities.<sup>20</sup> Mayer proposes the term "enlightened corporations", referring to corporations which deliver their stated purpose by integrating and balancing the six components of capital: human capital,

7 See, e.g., BEATE SJÅFJELL, *Why Law Matters: Corporate Social Irresponsibility and the Futility of Voluntary Climate Change Mitigation*, *European Company Law* 8/2011, p. 57 s.

8 European Commission, *A renewed strategy 2011-14 for Corporate Social Responsibility* (COM [2011] 681), p. 6. The European Commission currently undertakes to review its corporate governance approach again (see below, II.2).

9 See PETER FORSTMOSER, *Corporate Social Responsibility, eine (neue) Rechtspflicht für Publikumsgesellschaften?*, in: Waldburger/Sester/Peter/Baer (eds.), *Law & Economics: Festschrift für Peter Nobel zum 70. Geburtstag*, Bern 2015, p. 158.

10 ROLF H. WEBER, *Corporate Social Responsibility as a Gap-Filling Instrument?*, in: Newell (ed.), *Corporate Social Responsibility: Challenges, Benefits and Impact on Business Performance*, New York 2014, p. 87.

11 See generally ÉLODIE BÉTHOUX / CLAUDE DIDRY / ARNAUD MIAS, *What Codes of Conduct Tell Us: corporate social responsibility and the nature of the multinational corporation*, *Corporate Governance: An International Review* 15/2007, p. 77.

12 World Business Council for Sustainable Development, *Corporate Social Responsibility: Meeting Changing Expectations*, 1999.

13 MILTON FRIEDMAN, *Capitalism and Freedom*, Chicago 1962, p. 112. It must be noted that FRIEDMAN did not entirely exclude the consideration of other interests than making profits in the interest of the owners of the corporation by stating that a corporate executive is also responsible to conform to the basic rules of society, both those embodied in law and ethical custom, see KAUFMANN (fn. 5), p. 5.

14 See, e.g., WILLIAM BRADFORD, *Beyond Good and Evil: The Commensurability of Corporate Profits and Human Rights* *Notre Dame Journal of Law, Ethics & Public Policy* 2012, p. 148. See also ERIC POSNER, *Milton Friedman Was Wrong*, *The Atlantic*, 22 August 2019.

15 BEATE SJÅFJELL, *Beyond Climate Risk: Integrating Sustainability into the Duties of the Corporate Bond*, *Deakin Law Review* 23/2018, p. 53.

16 KAUFMANN (fn. 5), p. 6 s.; MARTIN PETRIN, *Reconceptualizing the Theory of the Firm – From Nature to Function*, *Penn State Law Review* 2013, p. 46; RASHID BAHAR, *Responsabilité sociétale des entreprises en droit de la société anonyme: entre devoir des organes et nouvelle technique de réglementation*, *ZSR* 139/2020 II, p. 281 (referring to the "grandeur et décadence de la shareholder value"); MATHIEU BLANC, *Corporate Purpose and Board of Directors: Means and Ends of Corporate Governance*, *SZW* 2020, p. 228.

17 See, e.g., DAVID MONSMA, *Equal Rights, Governance, and the Environmental Justice Principles in Corporate Social Responsibility*, *Ecology Law Quarterly* 33/2006, p. 477.

18 JOHN ELKINGTON, *Cannibals with Forks: the Triple Bottom Line of 21st Century Business*, Oxford 1997; WEBER, *Corporate Social Responsibility* (fn. 10), p. 89.

19 Regierungskommission, *Deutscher Corporate Governance Kodex* (German Corporate Governance Code, version of 16 December 2019), *Preamble*.

20 COLIN MAYER, *Reinventing the corporation*, *Journal of the British Academy* 4/2016, p. 53.

intellectual capital, material capital, natural capital (i.e., the environment, land and nature), social capital, and financial capital.<sup>21</sup> This concept encompasses a much wider range of interests than is usually considered in business practice, given that presently, corporations only report their net worth in relation to their financial and material capital, but not in relation to the other four components of capital.<sup>22</sup> With respect to natural capital in particular, Mayer states that “[t]here is one form of capital that the corporation has not produced at all to date and which, on the contrary, it has consumed voraciously, and that is natural capital. One of the reasons why we stand on the precipice of environmental disaster is its failure to do so.”<sup>23</sup>

12 Going beyond a scholarly debate, CSR narratives have reached board rooms. In August 2019, the Business Roundtable, a group of leading US chief executives, issued its revised “Statement on the Purpose of a Corporation”. The statement highlights that each of a corporation’s stakeholders – which are delineated as including customers, employees, suppliers, communities and shareholders – is “essential”, and contains a (vague) commitment to environmental protection by a reference to “embracing sustainable business practices”.<sup>24</sup> This expression of view gained widespread attention because it implicitly challenges the common social norm of shareholder primacy.<sup>25</sup> Shortly after, the World Economic Forum published a manifesto urging companies to move away from the model of “shareholder capitalism” as realized in most Western economies to “stakeholder capitalism”, a model which positions private corporations as “trustees of society” in response to today’s social and environmental problems.<sup>26</sup>

13 Yet, although the stakeholder movement has become quite strong, empirical evidence analyzing the behavior of leadership in corporations is not very encouraging.<sup>27</sup> Further, private sector references to the need to protect the environment are (more often than not) character-

ized by being vague or by being framed as “aspirational goals”, leading to criticism accusing such practices of “greenwashing”.<sup>28</sup>

### 3. Broadened Responsibility Concepts

Traditionally, international law is understood to be applicable only to Nation States, but typically not (directly) to businesses and other private actors. Yet, over the last two decades, its influence has also grown for so-called horizontal relations between commercially acting entities.<sup>29</sup> The fact that multinational corporations are operating across national borders calls for efforts to fill the so-called regulatory vacuum effect caused by the limitation of national governments’ power to their localized sphere.<sup>30</sup>

The United Nations has been a key driver of attempts to implement environmental, social and governance (ESG) issues into the objectives of corporations and institutions. Focusing in particular on investors, a 2019 report commissioned by the UN Environment Program Finance Initiative (UNEP FI) held that according to empirical and academic evidence, ESG issues are financially material<sup>31</sup> and must therefore be incorporated into investment analysis and decision-making processes.<sup>32</sup> The recognition of materiality is a paradigm change, considering that ESG issues were typically perceived as largely “immaterial” on a company’s success.<sup>33</sup> Implementing this new understanding, the UN Principles for Responsible Investment (UN PRI) provide six principles for integrating ESG issues into investment practice.<sup>34</sup> Companies are expected to incorporate environmental and social responsibility into their decision-making processes as part of a balanced assessment of business risks and opportunities.<sup>35</sup>

The perceived lack of corporate accountability with respect to social and environmental issues increasingly

21 MAYER (fn. 20), p. 65.

22 MAYER (fn. 20), p. 66.

23 MAYER (fn. 20), p. 66.

24 Business Roundtable, Statement on the Purpose of a Corporation, 2019.

25 ALIA. ZAIDI, Mandates for Action: Corporate Governance Meets Climate Change, *Stanford Law Review Online* 72/2020, p. 124.

26 KLAUS SCHWAB, Davos Manifesto 2020: The Universal Purpose of a Company in the Fourth Industrial Revolution, [weforum.org](http://weforum.org), 2 December 2019; KLAUS SCHWAB, Why we need the ‘Davos Manifesto’ for a better kind of capitalism, [weforum.org](http://weforum.org), 1 December 2019.

27 See LUCIAN A. BEBCHUK / KOBI KASTIEL / ROBERTA TALLARITA, For Whom Corporate Leaders Bargain, 2020 (finding empirical evidence that in private equity acquisitions, corporate leaders make very little use of their power to negotiate for stakeholder protections, but instead use their bargaining power to obtain benefits for shareholders, executives, and directors).

28 See generally SEBASTIÃO V. DE FREITAS NETTO / MARCOS F. FALCÃO SOBRAL / ANA R. BEZERRA RIBEIRO / GLEIBSON R. DA LUZ SOARES, Concepts and forms of greenwashing: a systematic review, *Environmental Sciences Europe* 32:19/2020.

29 See generally BENEDICT KINGSBURY, The International Legal Order, in: Tushnet/Cane (eds.), *The Oxford Handbook of Legal Studies*, Oxford 2003, p. 271 ss.

30 WEBER, Corporate Social Responsibility (fn. 10), p. 90.

31 In the sense that they are likely to affect financial performance.

32 RORY SULLIVAN / WILL MARTINDALE / ELODIA FELLER / MARGARITA PIROVSKA / REBECCA ELLIOTT, Fiduciary Duty in the 21st Century. Final Report, 2019, p. 8.

33 See, e.g., PAUL RISSMAN / DIANA KEARNEY, Rise of the Shadow ESG Regulators: Investment Advisers, Sustainability Accounting, and Their Effects on Corporate Social Responsibility, *Environmental Law Reporter* 49/2019, p. 10160.

34 See UN PRI, About the PRI. The six principles represent a “voluntary and aspirational” set of possible actions for investors.

35 See THOMAS CLARKE, The Widening Scope of Directors’ Duties: Closing the Gap Between Legal Obligation and Enforcement Practice, *Seattle University Law Review* 39/2016, p. 570.

prompts calls for regulation. For instance, in December 2019, dozens of legal scholars signed a statement entitled “Corporate Governance for Sustainability” suggesting the introduction of a legally binding obligation for directors to “develop, disclose and implement, on behalf of the company, a forward-looking corporate sustainability strategy that identifies and addresses material environment and social issues and significant impacts connected to the company’s business model, operations and supply chain”.<sup>36</sup> Further, among other related regulatory projects, the European Commission has recently launched an initiative to improve the European Union regulatory framework on corporate governance and company law, aiming to “better align the interests of companies, their shareholders, managers, stakeholders and society”.<sup>37</sup>

- 17 Legal literature points to the ability of already existing laws and legal concepts to adapt to changed circumstances and societal priorities with regard to climate change.<sup>38</sup> According to CLARKE, the scope of directors’ duties has broadened over the last few years due to the impact of international, national, market, business and civil society campaigns for corporate social and environmental sustainability.<sup>39</sup>

#### 4. Hardening Soft Law Standards

- 18 The issue of classifying CSR guidelines has caused controversy amongst legal scholars. Should CSR frameworks formally be qualified as “hard law”, “soft law”, or rather as a hybrid form composed of various co-existing regulatory approaches?<sup>40</sup> This discussion leads to the following question: to what extent can normative provisions be developed outside traditional forms of international and national legal sources (such as treaties, constitutions, regulations, etc.)? Indeed, CSR can go *beyond* the law, be brought *through* the law, or serve as a control mechanism *for* the law.<sup>41</sup> In order to overcome the partly

ambiguous character of CSR guidelines, new theories have been developed in order to extend an increased legal quality to such guidelines.<sup>42</sup>

Soft law can be described as “non-binding rules that have legal consequences because they shape states’ expectations as to what constitutes compliant behavior”.<sup>43</sup> In the last two decades, soft law gained substantial importance. Due to fast-moving societal developments, an easy and informal development and application of standards would seem desirable. Generally, the reliability of soft law depends on its acceptability in the concerned community. Indeed, rules created by stakeholders can be efficient since they respond to real needs by mirroring the aims of society. Meaningful self-regulation provides the opportunity to adapt the regulatory framework to the ever-changing environment in a flexible way.<sup>44</sup> The positive aspects of soft law must, however, be balanced against substantial drawbacks. Voluntary guidelines risk being ineffective for lack of enforcement measures and thus dependency on companies’ willingness to adhere to them.<sup>45</sup> A related risk is the possibility of companies claiming to be compliant with certain guidelines (for instance, the UN PRI) without actually implementing them, given that non-compliance does not have serious consequences.<sup>46</sup>

The traditional dichotomy between hard law and soft law must be overcome.<sup>47</sup> Even if some of its weaknesses cannot be overlooked (in particular, with respect to limited enforcement measures), soft law is suitable to be applied intelligently and promptly to deal with changing circumstances.<sup>48</sup> Notwithstanding the fact that a universally accepted theory as to the legal quality of private rule-making has not yet been developed, it can be said that soft law often affects behavior and might in time solidify into hard law, meaning that soft law is apt to be transformed or transplanted into hard law.<sup>49</sup>

Soft law also shapes the expectations and decisions of global actors participating in international relations. Such kind of development particularly occurs if private rulemaking is supported by governmental inputs in any

36 ANDREW JOHNSTON et al., *Corporate Governance for Sustainability Statement*, 7 January 2020.

37 See European Commission, *Sustainable Corporate Governance*. See also below, III.5.

38 See, e.g., ROLF H. WEBER / ANDREAS HÖSLI, *Climate Change Liability: Comparing Risks for Directors in Jurisdictions of the Common and Civil Law*, *Climate Law (CLL)* 10/2020, p. 195, with references; SARAH BARKER / ELLIE MULHOLLAND, *Directors’ Liability and Climate Risk: Comparative Paper: Australia, Canada, South Africa, and the United Kingdom*, 2019, p. 17.

39 CLARKE (fn. 35), p. 545 ss.

40 See, e.g., ROLF H. WEBER, *Realizing a New Global Cyberspace Framework, Normative Foundations and Guiding Principles*, Berlin 2014, p. 90 s.; VALENTIN JENTSCH, *Corporate Social Responsibility between Self-Regulation and Government Intervention: Monitoring, Enforcement and Transparency*, *European Business Law Review* 2020, p. 286.

41 See generally HOWARD R. BOWEN, *Social Responsibilities of the Businessman*, New York 1953.

42 WEBER, *Realizing a New Global Cyberspace Framework* (fn. 40), p. 91 ss., JENTSCH (fn. 40), p. 287 ss.

43 ANDREW T. GUZMAN / TIMOTHY L. MEYER, *International Soft Law*, *The Journal of Legal Analysis* 2/2010, p. 175.

44 WEBER, *Realizing a New Global Cyberspace Framework* (fn. 40), p. 27.

45 E.g., LISE SMIT et al., *Study on due diligence requirements through the supply chain*, 2020, p. 556.

46 SMIT et al. (fn. 45), p. 556.

47 ROLF H. WEBER, *Overcoming the Hard Law/Soft Law Dichotomy in Times of (Financial) Crises*, *Journal of Governance and Regulation* 1/2012, p. 8.

48 CLARKE (fn. 35), p. 571.

49 CLARKE (fn. 35), p. 571; WEBER, *Corporate Social Responsibility* (fn. 10), p. 90.

form of co-regulation. The respective models are designed in a way that the government implements the general framework which is then developed further by the private sector. Indeed, the behavior of multinational corporations being governed by governmental guidelines and by CSR rules can determine the manner in which activities of businesses are conducted worldwide.<sup>50</sup> In light of the foregoing, turning to the global issue of climate change, the following discussion of corporate responsibility in the climate context needs to address the soft law impacts on corporate duties.

### III. Corporate Climate Responsibility: Contours of a New Governance Issue

#### 1. Introducing CCR: Three Hypotheses

22 Introducing CCR rightfully raises the question why such a new term or concept would be helpful or necessary in the first place. Three hypotheses form the basis for the rationale:

- Fully acknowledging that many (often interrelated) social and environmental global challenges exist, climate change is arguably “the grandest of challenges facing humanity”<sup>51</sup>, with co-benefits for efforts to address other issues in case of strong climate action. Compared to some other issues, climate change is a particularly time-critical and large-scale problem, considering the need for unprecedented and “rapid and far-reaching transformations” in essentially all business sectors.<sup>52</sup>
- While a number of concepts dealing with corporate social and environmental responsibility already exist, most importantly CSR, ESG and “sustainability” concepts, none of these deal with climate change specifically. These “broader” concepts, while attempting to capture many other societal and environmental issues, could be at risk of not being specific enough to be of actual use in the context of meaningful climate change mitigation in the private sector, thus potentially even “blurring” the latter.
- Going beyond a purely legal view, CCR attempts to equally assess the impacts of relevant market developments, which – possibly again in contrast to

other global issues – are key drivers in the climate change context (see below, III.2).

#### 2. Drivers of the New Focus on Climate Change

Climate change has become a major political and economic issue over the last few years. According to the World Economic Forum’s *Global Risk Report 2021* which captures the perceived global risks landscape, the risk of climate action failure ranks second in terms of likelihood as well as in terms of impact.<sup>53</sup> While the COVID-19 pandemic has attracted major attention in 2020 and beyond, climate change remains a top catastrophic risk, especially as global cooperation weakens.<sup>54</sup>

Various developments in different areas influence the behavior of decision-makers in companies relating to climate change. With respect to CCR, the following graph gives an insight into the multifaceted situation:<sup>55</sup>



The international legal framework on climate change provides a point of reference for corporations in terms of response measures (see below III.3). The increasing recognition of significant business risks linked to climate change as well as emerging litigation contribute to pressure on corporations (see below III.4). These developments are complemented by discussions with respect to a broadening of a corporation’s responsibility towards society and the environment (see above II.2, II.3, below, III.5).

50 WEBER, Corporate Social Responsibility (fn. 10), p. 87.

51 CHRISTOPHER WRIGHT / DANIEL NYBERG, An Inconvenient Truth: How Organizations Translate Climate Change into Business as Usual, *Academy of Management Journal* 60/2017, p. 1633.

52 Intergovernmental Panel on Climate Change (IPCC), 2018: Summary for Policymakers, in: *Global Warming of 1.5°C. An IPCC Special Report on the impacts of global warming of 1.5°C above pre-industrial levels and related global greenhouse gas emission pathways, in the context of strengthening the global response to the threat of climate change, sustainable development, and efforts to eradicate poverty*, C.2, p. 15.

53 World Economic Forum (WEF), *The Global Risks Report 2021*, 2021, p. 3 (the top risk in terms of likelihood being extreme weather, and the top risk in terms of impact being infectious diseases, in the face of COVID-19).

54 WEF (fn. 53), p. 6.

55 This graph has been inspired by CLARKE (fn. 35), p. 547 and amended by the authors to specifically reflect CCR.

### 3. The Business Response to the Regulatory Framework

- 26 In 2015, two important milestones in terms of global sustainability policy were achieved: the UN 2030 Agenda for Sustainable Development<sup>56</sup>, which sets out 17 Sustainable Development Goals (SDGs)<sup>57</sup>, and, more importantly in the climate change context, the Paris Agreement.<sup>58</sup> The goals of the Paris Agreement consist of limiting global temperature increase at “well below” 2°C or preferably 1.5°C above pre-industrial levels (art. 2[1][a]), adapting to a warming world (art. 2[1][b]), as well as aligning finance flows with the first two goals (art. 2[1][c]). Although legal obligations for corporations to limit or reduce their GHG emissions cannot easily be drawn from them, both the SDGs as well as the Paris Agreement have at least been echoed by the private sector. Companies and business organizations have voiced broad support for the SDGs and the Paris Agreement, albeit mostly in terms of statements, “commitments” and initiatives with unclear legal value. For instance, members of the Net-Zero Asset Owner Alliance, a United Nations convened group of large institutional investors representing trillions in assets under management, “committed” to transitioning their investment portfolios to net-zero GHG emissions by 2050, including by establishing intermediate targets every five years in line with the Paris Agreement.<sup>59</sup>
- 27 Another impetus for more business attention to climate change is the expectation of a tightening of the relevant regulatory frameworks worldwide.<sup>60</sup> This is particularly the case for the European Union, where efforts are currently underway to integrate sustainability (to include climate change considerations) into corporate decision-making by way of new regulations, mainly (but not only) in the financial sector (see also below, III.4).<sup>61</sup>

56 UN General Assembly Resolution 70/1 of 25 September 2015 (Transforming our world: the 2030 Agenda for Sustainable Development).

57 Goal 13 (Climate Action) is to take urgent action to combat climate change and its impacts, whilst acknowledging that the “United Nations Framework Convention on Climate Change [UNFCCC, United Nations, Treaty Series, vol. 1771, No. 30822] is the primary international, intergovernmental forum for negotiating the global response to climate change” (fn. 56, p.8).

58 Paris Agreement to the United Nations Framework Convention on Climate Change, 12 December 2015 (T.I.A.S. No. 16-1104).

59 UN Environment Programme Finance Initiative (UNEP FI), United Nations-Convened Net-Zero Asset Owner Alliance. For other examples see WEBER/HÖSLI (fn. 38), p. 163 ss.

60 See, e.g., Mercer, *European Asset Allocation Survey 2019*, 2019, p. 29.

61 See WEBER/HÖSLI (fn. 38), p. 192 ss. (discussing in particular the European Commission’s Action Plan: Financing Sustainable Growth [European Commission, ‘Action Plan: Financing Sustainable Growth’, Brussels, 8 March 2018, COM(2018) 97 final]).

### 4. Climate Change as a Business Risk

From a business perspective, climate change risks are commonly divided into two main categories: physical risks and transition risks.<sup>62</sup> Physical risks arise from climate-related events, whether “acute” (e.g., bushfires) or “chronic” (e.g., ocean acidification). Transition risks relate to the global transition to a “lower-carbon” economy and encompass five sub-categories, namely (i) policy risks arising from the expected tightening of the relevant regulatory frameworks (e.g., increasing CO<sub>2</sub> taxes); (ii) litigation risks due to climate change litigation (against corporations); (iii) technology risks from breakthroughs in ‘clean’ technologies; (iv) market-related risks from changes in consumer behavior; and (v) reputation risks arising from public pressure.<sup>63</sup>

Numerous international financial institutions, central banks and international organizations have recently highlighted the need to put more emphasis on climate-related risks. For instance, in its 2020 “Green Swan” report, the Bank for International Settlements identified climate-related risks as “potentially extremely disruptive events that could be behind the next systemic financial crisis” and stressed the need for central banks to integrate these risks into financial stability monitoring.<sup>64</sup> Serious concerns over the impacts of climate change on the economy have prompted the launch of the Network of Central Banks and Supervisors for Greening the Financial System (NGFS) in 2017.<sup>65</sup> As regards regulators and supervisors at the national level, authorities in a number of countries including the United Kingdom, Australia, and France have communicated specific climate change expectations to market participants in their respective jurisdictions.<sup>66</sup> Investors, in particular institutional investors such as pension funds and large asset managers, are key drivers of the trend towards more regard for climate change-related issues. A number of investor coalitions and initiatives have been formed, some of which in cooperation with international organizations (see above, III.3).

62 See WEBER/HÖSLI (fn. 38), p. 154 s., with further references.

63 See Task Force on Climate-related Financial Disclosures (TCFD), *Final Report – Recommendations of the Task Force on Climate related Financial Disclosures*, 2017, p. 5 s.

64 PATRICK BOLTON / MORGAN DESPERES / LUIZ A. PEREIRA DA SILVA / FRÉDÉRIC SAMAMA / ROMAIN SVARTZMAN, *The green swan. Central Banking and financial stability in the age of climate change*, 2020, p. iii.

65 www.ngfs.net. Members of the NGFS, which include the European Central Bank (ECB), the International Monetary Fund (IMF), and many others, acknowledge climate change as a source of financial risk (NGFS, *First Progress Report*, 2018, p. 3).

66 In relation to the United Kingdom and Australia, see WEBER/HÖSLI (fn. 38), p. 172 ss.

30 Notwithstanding the fact that many companies as well as investors are aware of the significant economic effects of climate change, indications that the respective climate-related risks are currently not sufficiently recognized cannot be overlooked. Consequently, these risks are not adequately reflected in asset prices, which exposes corporations and investors to so-called risks of “stranded assets”, that is, sharp and sudden value losses in fossil fuel assets.<sup>67</sup>

31 Practice has also shown the rise of climate change litigation against corporations.<sup>68</sup> Lawsuits are brought in particular where it is claimed that a lack of sensitivity for climate change aspects has led to a drop in share prices or even bankruptcy (constituting a damage for shareholders or creditors), or where historical contributions to climate change have allegedly caused damage to a third party not related to the corporation.<sup>69</sup> While climate change litigation against corporations first emerged in jurisdictions of the common law (mainly the United States, the United Kingdom, and Australia), recent years have seen the first cases in European civil law jurisdictions (in particular, the German tort case *Lliuya v RWE*<sup>70</sup>).<sup>71</sup> Climate change litigation against private corporations in Europe is, however, still in its infancy.<sup>72</sup>

## 5. Key Elements of CCR: Disclosure and Due Diligence

32 Governance relates to the responsibilities imposed on corporate decision-makers in most legal systems around the world. Fiduciary duties are the core framework governing the discretion of directors in common-law jurisdictions, and are typically expressed in equivalent statutory provisions in civil law countries.<sup>73</sup> As one of the two key elements (the other being the duty of loyalty), the duty of care requires members of the board to act on a fully informed basis, in good faith, and with due diligence and care.<sup>74</sup> Generally, the duty of care is a standard of reference which is the behaviour that can reasonably be expected from a prudent person under the given

or comparable circumstances.<sup>75</sup> This standard is not static, but evolves as society changes and in response to the need for a transition to an environmentally, economically and socially sustainable financial system.<sup>76</sup> Accordingly, a corporation’s strategic response to climate change must include a robust engagement with its fiduciary duties and other governance constraints.<sup>77</sup>

While narrower, traditional framings of the corporate purpose tend to focus on shareholder wealth maximization, newer conceptions give way to a broader set of emerging duties which are not only owed to shareholders but to a more comprehensive group of stakeholders (see above, II.2, II.3).<sup>78</sup> This widening scope of corporate decision-makers’ duties includes a responsibility to give adequate weight to climate change risks, given their significance.<sup>79</sup> Grasping the interplay between corporate governance and climate change requires an understanding of what corporate duties demand from business leaders in the face of this systemic environmental risk.<sup>80</sup> Corporate duties mandating greater attention to climate change are, by and large, non-existent or at least rather vague or general in nature.<sup>81</sup> Accordingly, the fast emergence of soft law dealing specifically with climate change related issues is apparent. In this context, the work of the Task Force on Climate-Related Financial Disclosure (TCFD) is particularly important. This industry-led expert group was initiated by the Financial Stability Board in December 2015 in order to develop recommendations for consistent disclosures to assist financial market participants understand material climate-related risks.<sup>82</sup>

Two core elements of CCR can be identified: transparency and due diligence.<sup>83</sup> First, a sound understanding of the impacts (both current and anticipated) of climate change on a specific company is required. The TCFD recommends to apply a so-called scenario analysis, which entails a process of (1) ensuring that adequate governance is in place, (2) assessing materiality of climate-related risks, (3) identifying and defining a range of scenarios, (4) evaluating business impacts (on operating costs, revenues, supply chains, etc.), (5) identifying potential responses, and (6) documenting and disclosure.<sup>84</sup> In 2017, the TCFD

67 See generally BEN CALDECOTT, Introduction to special issue: Stranded assets and the environment, *Journal of Sustainable Finance and Investment* 1/2017, p. 1; WEBER/HÖSLI (fn. 38), p. 155 s.

68 JAVIER SOLANA, Climate Breakdown Litigation in Financial Systems: A Typology, *Transnational Environmental Law* 9/2020, p. 103.

69 See WEBER/HÖSLI (fn. 38), p. 158 ss.

70 Decision of the Landgericht Essen 2 O 285 of 15 December 2016 (*Lliuya v. RWE*; printed in NVwZ 2017, p. 234), discussed in WEBER/HÖSLI (fn. 38), p. 191 s.

71 WEBER/HÖSLI (fn. 38), 194.

72 MARTIN SPITZER / BERNHARD BURTSCHER, Liability for Climate Change: Cases, Challenges and Concepts, *Journal of European Tort Law* 8/2017, p. 176.

73 SULLIVAN et al. (fn. 32), 11.

74 OECD, *Principles of Corporate Governance*, 2015, p. 46.

75 OECD (fn. 74), p. 46.

76 See SULLIVAN et al. (fn. 32), p. 12.

77 ZAIDI (fn. 25), p. 131.

78 ZAIDI (fn. 25), p. 124.

79 See CLARKE (fn. 35), 541.

80 ZAIDI (fn. 25), p. 126.

81 See WEBER/HÖSLI (fn. 38), p. 172 ss.

82 TCFD, *Final Report* (fn. 63), p. 2.

83 See generally ANDREAS HÖSLI / ROLF H. WEBER, *Climate Change Reporting and Due Diligence: Frontiers of Corporate Climate Governance*, forthcoming 2021.

84 TCFD, *The Use of Scenario Analysis in Disclosure of Climate-Related risks and Opportunities*, 2017, p. 7.



presented detailed recommendations on climate-related disclosures (hereinafter “TCFD Recommendations”) that are applicable to organizations across business sectors (including the financial sector) and jurisdictions.<sup>85</sup> The TCFD Recommendations are structured around four thematic areas that stand for the main elements of how corporations operate: governance, strategy, risk management, and metrics and targets.<sup>86</sup> Importantly, the transition to a lower-carbon economy not only entails risk, but also offers significant business opportunities which should equally be assessed in the processes described.<sup>87</sup>

35 The second core aspect of CCR relates to due diligence. The concept of due diligence to identify, prevent, mitigate and account for harmful corporate impacts on human rights and the environment was promoted by the 2011 UN Guiding Principles on Business and Human Rights (UNGPs) and then incorporated into the 1976 OECD Guidelines for Multinational Enterprises (OECD Guidelines)<sup>88</sup> to expressly extend to other areas of responsible business conduct such as environment and climate change, bribery, and consumer rights.<sup>89</sup> In Chapter VI on the environment, the OECD Guidelines recommend that companies establish and maintain an environmental management system. While not expressly referring to climate change in the current 2011 version, the OECD Guidelines encourage improving corporate environmental performance at the level of the enterprise and, where appropriate, of its supply chain. This shall be done, among other things, by developing products and services that reduce GHG emissions and by promoting awareness among customers of the environmental implications of the products and services offered through accurate information on GHG emissions (and other environmental issues such as biodiversity).<sup>90</sup> Countries adhering to the OECD Guidelines are under an obligation to establish National Contact Points (NCPs), to which complaints alleging breaches of the guidelines can be made; the OECD Guidelines are therefore *not* a purely voluntary instrument.<sup>91</sup> Indeed, climate change cases have already been filed with OECD NCPs. The Netherlands NCP, in April 2019, clarified that under the OECD Guidelines, companies are expected to conduct climate change due diligence both with respect to their own emissions as well as regarding emissions along the supply chain.<sup>92</sup>

85 TCFD, final report (fn. 63), p. iii.

86 TCFD, final report (fn. 63), p. 14.

87 TCFD, final report (fn. 63), p. 6 s.

88 In addition, in 2018, the OECD released a more specific “Due Diligence Guidance for Responsible Business Conduct”, 2018.

89 See SMIT et al. (fn. 45), p. 36.

90 SMIT et al. (fn. 45), p. 43.

91 KAUFMANN (fn. 5), p. 14.

92 The Netherlands NCP, *4 NGOs versus ING*, Final Statement, 19 April 2019. The Final Statement states that “[u]nder the terms of the OECD

Acknowledging transparency as one way to incentivize 36  
companies to do no harm, embedding sustainability issues (including climate change) into corporate duties of care is arguably a more effective way to enhance responsible corporate behavior.<sup>93</sup> Nevertheless, compared to disclosure, due diligence has so far received less attention in the climate change context. Although large companies commonly assess environmental impacts, including climate change, in their due diligence, the term “climate change due diligence” is so far rarely used, and human rights and climate change processes are often limited to their respective “silos”.<sup>94</sup>

International climate-related soft law standards are be- 37  
ginning to “solidify” into hard law. The first “wave” of this development relates to disclosure standards. For instance, in September 2020, New Zealand announced to make climate-related financial disclosures mandatory for some organizations including larger financial institutions, in line with the TCFD Recommendations.<sup>95</sup> The European Union started to incorporate the TCFD Recommendations into its regulations and guidelines.<sup>96</sup> In contrast to disclosure, where the TCFD Recommendations provide a rather detailed and climate-specific framework, a comparable climate due diligence framework does not exist. In most countries, there currently is no general duty on companies to undertake due diligence for their environmental (and human rights) harms, but this is changing. For instance, in 2017, France introduced mandatory due-diligence requirements with respect to the social and environmental impacts (implicitly including climate change) of the operations of large French companies.<sup>97</sup> In 2020, building on the UNGPs and the OECD Guidelines, the European Union announced plans to propose new mandatory human rights and environmental due diligence legislation. In Switzerland, in November 2020, a popular initiative which would have imposed stricter rules (including due diligence and liability) on

Guidelines companies are expected to conduct a due diligence process in respect of their environmental impact, including climate impact. This relates not only to their own negative environmental impact, but also to the impact in their value chain” (p. 3).

93 See SMIT et al. (fn. 45), p. 37.

94 SMIT et al. (fn. 45), p. 16.

95 Ministry for the Environment/Manatu Mo Te Taiao, Mandatory climate-related financial disclosures; concerning Switzerland, see Swiss Financial Market Supervisory Authority (FINMA), Transparency obligations for climate risks – FINMA opens consultation, 10 November 2020.

96 See, e.g., European Commission, Guidelines on reporting climate-related financial information, C(2019) 4490 final. Further, the Non-Financial Reporting Directive (Directive [EU] 2014/95/EU amending Directive [EU] 2013/34 as regards disclosure of non-financial and diversity information by certain large undertakings and groups [NFRD]) currently undergoes revision.

97 *Loi de Vigilance* du 27 mars 2017 relative au devoir de vigilance des sociétés mères et des entreprises donneuses d’ordre (Loi n° 2017-399), discussed in WEBER/HÖSLI (fn. 38), p. 186 ss.

large Swiss based corporations in terms of human rights and environmental standards failed by a very narrow margin, nevertheless paving the way for mandatory disclosure requirements.<sup>98</sup>

## 6. Legal Quality of CCR

- 38 Although there is no generally valid legal qualification of CSR standards (see above, II.4), guidelines such as the TCFD Recommendations and the OECD Guidelines are in principle suitable to be used to specify a certain level of care expected under openly framed concepts such as duties of care.
- 39 As soon as such guidelines are referred to in the context of interpreting a legal duty, compliance with them becomes a matter of “hard law”, even if their legal character is not part of the traditional normative system.<sup>99</sup> While the issue of liability has been discussed primarily in the field of human rights violations<sup>100</sup>, an increasing body of literature analyzes concepts of climate change corporate liability.<sup>101</sup> Soft law standards assisting to make the scope of openly framed corporate duties more specific gain importance in practice and contribute to the “hardening” of such guidelines.
- 40 In any event, even with a relatively narrow conception of the corporate purpose, sound governance demands attentiveness to and action on climate change issues.<sup>102</sup> As a result, corporations are confronted with new expectations in the execution of their activities. In particular, a

98 Although a majority of the Swiss electorate (50.7%) had voted in favour of the Responsible Business Initiative, the second, “federalist” requirement to amend the constitution, a majority of the states, was not reached. As a result of the rejection, a counter-proposal introducing certain mandatory transparency rules will go forward. Generally with respect to human rights and environmental corporate responsibility in Switzerland, see DAMIANO CANAPA / EVELYNE SCHMID / ELENA CIMA, “Entreprises responsables”: trois malentendus, Jusletter of 23 November 2020.

99 See WEBER, Overcoming the Hard Law/Soft Law Dichotomy (fn. 47), p. 8 ss.

100 E.g., ROLF H. WEBER / RAINER BAISCH, Liability of Parent Companies for Human Rights Violations of Subsidiaries, *European Business Law Review* 2016, p. 685.

101 See, e.g., SPITZER/BURTSCHER (fn. 72).

102 ZAIDI (fn. 25), p. 126.

number of legal scholars argue that in the discharge of their fiduciary duties, members of corporate boards are not only allowed, but even *required* to have regard to climate related risks, at least to the extent that they represent financially material risks.<sup>103</sup>

## IV. Conclusion and Outlook

In the absence of comprehensive, specific and enforceable obligations for corporations to reduce or limit their GHG emissions, considerable efforts are currently being undertaken to develop international climate change-related guidelines and recommendations for the private sector. These instruments would typically be considered as soft law being suitable to be eventually transformed into hard law, a development which has already begun. While its concept and scope needs further refinement and discussion, CCR can serve as a basis to frame further discourse on corporate responsibility in the field of climate change.

The regulatory framework governing the behavior of corporate decision-makers in the climate change context is constantly developing. Accordingly, the extension of the relevant duties and obligations is a consequence of moving societal perceptions.

The COVID-19 pandemic is a reminder that major disruptions to business as usual can occur at any time. Similar to risks of global pandemics, scientists have been warning of climate change risks for decades. While it seems that these warnings are heard by governments and the corporate world more than in previous years, it still appears questionable whether the corporate response to climate change risks occurs coherently and swiftly. In this context, the work of the TCFD and international bodies including the OECD and the UN in developing widely applicable standards remains important.

103 See, e.g., NOEL HUTLEY / SEBASTIAN HARTFORD-DAVIS, *Climate Change and Directors’ Duties*, 2016, paras 12, 42 ss.; LISA BENJAMIN, *The Duty of Due Consideration in the Anthropocene: Climate Risk and English Directorial Duties*, *Carbon & Climate Law Review* 11/2017, p. 94 ss.; WEBER/HÖSLI (fn. 38), p. 188 s., with further reference.