Corporate Law, directors' duties and ESG interventions: Analysing pathways towards positive corporate impacts relating to ESG issues.

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Abstract

Considering the steps necessary to steer companies towards positive impacts in terms of environmental, social and governance (ESG) issues requires analysis of the way that corporate decisions are made, the effectiveness of existing initiatives to influence decision-making and the relationship that both have with corporate law itself. This article contributes to that process by considering the relationship that ESG initiatives have with corporate law. It provides an analysis of the tensions that can exist between ESG initiatives and directors' fiduciary duties, to investigate the threshold at which an 'upper limit' in ESG regulatory efficiency occurs. However it argues that directors' duties should not be viewed in isolation when consideration is given to ESG issues, as they are only one part of the broader legal construct of 'the company' – a construct that is predisposed towards negative outcomes for ESG concerns. It therefore argues that a broader approach is necessary and suggests pathways towards more effective development of law and regulation in this sphere.

Keywords: directors' duties, ESG, human rights, corporate decision-making, legal construct.

1. Introduction

Over the last forty to fifty years many of the initiatives, both legal and non-legal, that have had the purpose of influencing the decision-making of companies relating to environmental, social and governance (ESG) issues have taken place as reactions to the way that specific industries have been run and also in response to the corporate law and regulatory regimes to which they are subject. The diverse nature and volume of these initiatives creates challenges for the assessment of their effectiveness. However such evaluation is crucial in determining the most efficient and effective ways to steer corporate decision-making in the future. It is in this space that the analysis of this article is situated. It considers the relationship between the decision-making made within the legal construct known as 'the company' and ESG initiatives, to determine the real effect that those ESG initiatives have on the priorities of company directors.

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To do this it considers the key pillars of the corporate legal construct that can have an effect on ESG issues. As such it takes into account the directors' duty to 'act in the best interest of a company',[1] 'separate legal personality' and 'limited liability'. It is argued that these components operate in concert, in a manner which can predispose company directors to make decisions that ultimately have negative outcomes for ESG issues. Whilst much academic attention is given to directors' duties in isolation, this article argues that the failure to take into account other components of the corporate legal construct obfuscates the overall purpose of companies and as such the legal framework that determines how directors are ultimately obliged to make decisions relating to ESG issues.

The article considers the different types of ESG initiatives that have been introduced by international organisations, governments, NGOs and companies themselves with the purpose of analysing their influence *vis à vis* corporate decision-making. Reference is made to a series of interviews conducted by the author with heads of corporate responsibility at listed companies that engage actively with ESG issues. The interviews alongside reference to research from other researchers, provide the basis for an analysis of the current drivers and determinants in the relationship between ESG initiatives and the priorities in corporate decision-making. The interviews were designed to investigate the threshold at which ESG initiatives may be subject to limitations in terms of their influence on corporate decision-making in the short and long term.

The overall purpose of this analysis is to assist in the consideration of pathways for further reform within the field of ESG. In particular it seeks to assist in understanding the proportion of effort that should be allocated to developing further legal and non-legal initiatives that are extraneous to corporate law itself and the proportion of effort that should be devoted to addressing the underlying drivers or root causes of ESG issues which can, in part at least, be found within the legal construct of the corporation.

2. The Corporate Legal Construct – Understanding why Corporate Decision-Makers make the Decisions that they do.

This section considers the corporate legal construct of which directors' duties are a part. It explores the function that the duty, 'to act in the best interests of the company' has when viewed in conjunction with 'separate legal personality' and 'limited liability'; as a result it sheds light on the underlying drivers that affect corporate decision-making. It considers the relationship that all three factors

[1] This broad definition is adopted for the purposes of this article as it provides a *de facto* representation of the legal obligation that company directors have in jurisdictions around the globe; see Adolfo Paolini (ed), *Research Handbook on Directors' Duties,* (Cheltenham: Edward Elgar, 2014); Andrew Keay, *Directors' Duties,* 3rd edn (Bristol: Jordan Publishing, 2016); Beate Sjåfell, Andrew Johnston, Linn Anker-Sørensen, and David Millon, 'Shareholder Primacy: The Main Barrier to Sustainable Companies' in Beate Sjåfell and Benjamin J. Richardson (eds) *Company Law and Sustainability – Legal Barriers and Opportunities* (Cambridge: Cambridge University Press, 2015) 79-147

operating together can have on ESG strategies and as such explains why analysis of directors duties should not be taken in isolation when consideration is given to the development of initiatives designed to respond to ESG issues.[2]

The historical foundations of directors duties, separate legal personality and limited liability in the context of ESG concerns, can be traced back over 220 years to the American War of Independence, the conclusion of which meant that newly formed states needed a method of incorporating businesses.[3] In the absence of a monarch to grant the charters required for businesses to become incorporated, states in the United States adopted laws that enabled businesses to adopt the corporate form and as a result the birth of the modern corporation as we currently know it had taken place.

The success of that model led other countries to adopt similar regimes themselves. The French,[4] British,[5] and Germans,[6] all followed suite. The success of the corporate form for businesses subsequently spread throughout the world by colonisation, transplantation,[7] and more recently through globalisation.[8] In all jurisdictions it has included the core features of separate legal personality, limited liability and directors' duties;[9] all of which are highly significant in terms of the outcomes for ESG issues. As such each of these features will be reviewed here in turn.

One of the characteristics of separate legal personality is that any debts of the business are *prima facie* at least, those of the company itself and not those of its shareholders. Therefore it is understandable that business people see the corporate form as a highly desirable medium through which to conduct business. However, this can lead to decision-making that is ultimately pre-disposed to a higher levels of risk relating to ESG issues. This predisposition can be amplified when a parent company sets up subsidiary, as the parent company itself will not *prima facie* be directly liable for the debts or liabilities of that subsidiary.[10] Therefore the subsidiary can be used as vehicle through which commercial operations, that may have high risks for ESG concerns, can be conducted whilst restricting the liability of the parent company and its owners.

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[2] Stephen J. Turner, *A Global Environmental Right* (Abingdon: Earthscan by Routledge, 2014) 40-4.

[3] Ibid 39.

[4] Mads Andenas & Frank Wooldridge, *European Comparative Company Law* (Cambridge: Cambridge University Press, 2009) 283.

[5] Joint Stock Companies Act 1844 7 & 8 Vict. C. 110 & 111.

[6] Gesetz betreffend die Gesellschaften mit beschrankter Haftung (GmbHG); see Klaus J. Hopt 'Comparative Company Law' in Mathias Reimann & Reinhard Zimmerman (eds), *The Oxford Handbook of Comparative Law* (Oxford: Oxford University Press, 2009) 1164.

[7] Hideki Kanda and Curtis J. Milhaupt, 'Re-examining Legal Transplants: The Director's Fiduciary Duty in Japanese Corporate Law' (2003) 51 *Am. J. Comp. L.* 887; Gerald McAlinn (ed), *Japanese Business Law,* (Leiden: Kluwer Law International, 2007) 109.

[8] Company Law of the People's Republic of China (Revised in 2005). (Adopted at the Fifth Session of the Standing Committee of the Eighth National People's Congress on December 29, 1993).

[9] Turner (n 2, 40-4); UN Global Compact Research Library 'Sustainability and the Fiduciary Duty of Boards of Directors' (2015). Available at: https://www.unglobalcompact.org/library/3791 (accessed 9th April 2019).

[10] Peter T. Muchlinski, *Multinational Enterprises and the Law,* 2nd edn. (OUP, 2007) 45-79.

The capacity that companies have to limit the liability of their shareholders similarly has the function of providing a safe-haven for investors. As the personal liability of any investor is limited to the amount that they have subscribed to pay on the purchase of their shares, the directors of companies can potentially take greater risks *vis à vis* ESG issues without exposing that same level of risk to the shareholders. It can mean that where a company causes harm to a community or the environment as a result of its operations, injured parties can be left without compensation in the event that the business becomes insolvent. This also explains why limited liability companies are much more common than unlimited liability companies.

In the 1790s when the corporation in its contemporary sense first emerged in the US, there were significant debates as to the desirability of allowing companies to limit the liability of their shareholders.[11] However when the state of New Hampshire became the first to allow companies to limit liability, all the other states swiftly followed suite.[12] In the UK, although businesses were allowed to incorporate from 1844 onwards, it was not until 1855 that Parliament passed legislation which allowed companies to limit liability.[13]

Both separate legal personality and limited liability would not have the same capacity to attract investors if company law did not also integrate strict rules for those running companies to ensure that funds invested are used for the purposes expected by investors. It is on this rationale that directors' duties have developed.[14] In fact the necessity that company funds are used for commercial purposes to facilitate financial returns on investments has meant that in many jurisdictions there are very strict consequences for directors that fall foul of those responsibilities.[15]

There have been attempts to influence or reinterpret the traditional duties that directors have towards companies, to ensure that human rights, environmental and governance issues are taken into account.[16] However, in all jurisdictions corporate law still requires the interests of the shareholders to be protected, and this is understandably translated in practice into the pursuit of commercial success.[17] Even where the interests of stakeholders other than shareholders are represented in the letter of the law, they are generally not provided with the

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[11] Harry G. Henn and John R. Alexander, *Laws of Corporations* 3rd edn (Minnesota: West Publishing Co. 1983) 25.
[12] Ibid
[13] Limited Liability Act 1855 (UK) 18 & 19 Vict. C. 133.
[14] L. C. B. Gower, *Principles of Modern Company Law* (London: Stevens and Sons, 1979) 255.
[15] See eg. Andenas & Wooldridge (n 4) 300-1; McAlinn (n 7) 109.
[16] See for example in the United Kingdom s.172 Companies Act; also under s166(2) of the Indian Companies Act (2013) directors have what appears to be a pluralistic responsibility to promote not only shareholders' interests but also those of communities and the environment; also in France at the time of writing the government is considering PACTE, a new code for companies. See https://www.gouvernement.fr/en/pacte-the-action-plan-for-business-growth-and-transformation (accessed 31st March 2019.)
[17] See Mihir Naniwadekar and Umakanth Varotil, 'The Stakeholder Approach Towards Directors' Duties Under Indian Company Law: A Comparative Analysis' in Mahendra Pal Singh (ed.) *The Indian Yearbook of Company Law* (OUP, 2016) 95-120.

means of redress that shareholders enjoy in the event that those interests are not promoted.[18] As a result, reducing overheads, in a manner that could potentially negatively affect the environment, communities or other stakeholders can be legitimate so long as it complies with the law of the jurisdiction concerned and is considered, on a commercial basis, to be in the best interests of the company. As a result of these component parts of the legal construct of the company in its current form, there are many instances where the result of companies' operations are water or air pollution, deforestation, poor labour standards, infringements of peoples' human rights, poor construction standards, communities being relocated, habitats being destroyed and ecosystems being permanently damaged or simply a heavy reliance on fossil fuels.

The integral function that directors' duties have alongside 'separate legal personality' and 'limited liability' in attracting and maintaining investment in companies means that alternative interpretations of directors' duties alone, face serious practical hurdles.[19] This is highlighted by those jurisdictions that have introduced mandatory requirements for company directors to take into account factors other than the financial interest of the company and shareholders' interests when making decisions (these are discussed in more detail in the next section).[20] It can be argued that without providing an alternative design concept of the overall legal construct of the company itself, that takes into account the role that each component part has in the protection of shareholders' interests, there can be limitations to the effectiveness of ESG initiatives.

3. The Relationship of ESG Interventions with the Legal Construct of the Company

This section considers the different types of ESG initiatives that have emerged with a view to determining their purpose *vis à vis* directors' fiduciary duties and the broader legal construct of the company. It does this by considering the mechanisms through which they are designed and determines whether each initiative can be categorised as a:

a) A Reputational Initiative - One which has the purpose of influencing the decision-making of companies through the effect that it can have on their reputation; or

[18] Ibid.

[19] See R. Edward Freeman, *Strategic Management: A Stakeholder Approach,* (Pitman, 1984) (Cambridge University Press, 2010); Christopher Stoney and Diana Winstanley, 'Stakeholding: Confustion or Utopia? Mapping the Conceptual Terrain' (2001) 38 J. Management Stud. 603; Jörg Andriof, Sandra Waddock, Bryan Husted, Sandra Sutherland (Eds), *Unfolding Stakeholder Thinking* (Taylor Francis, 2002); Andrew Keay, 'Stakeholder Theory in Corporate Law: Has it Got what it takes?' (2010) 9(3) Richmond. J. Global Law & Business 249-300; Sjåfell, Johnston, Anker-Sørensen, and Millon (n 2) 79-147.

[20] See S. 172 Companies Act (2006) United Kingdom; see John Edward Parkinson, *Corporate Power and Responsibility: Issues in the Theory of Company Law* (Oxford: Clarendon Press, 1997) 304ff.

b) A Legal Compliance Initiative – One which creates legislation that directly or indirectly affects corporate decision-making but which does not directly affect the core legal duty that companies have to make decisions which are in the best interests of the company; or

c) A Legal Construct Initiative – One which modifies or alters the duty that company directors' have to act in the best interests of the company or another aspect of the legal construct of the company.

This analysis provides the foundation for the latter stages of the article which considers the effects of these interventions in practice, their limitations and what that means for further development and reform.

3.1 International Organisations

Relevant initiatives by international organisations can be traced back to the 1970s when the UN was starting to take steps to respond to the unwanted ESG impacts of trans-national corporations (TNC).[21] Reports from that period include an attempt to develop an operable code of conduct for TNCs.[22] In 2000 the UN launched its Global Compact,[23] a voluntary membership scheme that corporations can subscribe to which requires that they report on the actions that they have adopted relating to ESG issues. This initiative has been widely accepted by many large corporations, states and the NGO community although its non-mandatory nature means that it is inherently limited as a solution.

Shortly after this, the UN Sub-Commission on the Promotion and Protection of Human Rights of the Economic and Social Council (UN Sub Commission) mandated a working group to develop a set of norms that transnational corporations would be obliged to follow. The norms (Draft Norms) that followed were approved by the UN Sub-Commission.[24] They did not however meet with the approval of many national governments and were particularly criticised for failing to adequately address the legal difficulties inherent in attempting to impose international human rights and international environmental law norms on non-state actors such as corporations.[25]

Following the rejection of the Draft Norms, the UN in 2005 appointed Prof. John Ruggie as the Special Representative of the Secretary General (SRSG) to consider how responsibility for human rights issues could be incorporated into business practice. Prof. Ruggie's work resulted in a final report which advocated a

[21] Early evidence is found in *Multinational Corporations in World Development* (United Nations, 1973).
[22] United Nations Code of Conduct on Transnational Corporations. See 'Official Records of the Economic and Social Council' (E/5655, E/C.10/6. 59th Session, Supplement No 12).
[23] United Nations Global Compact. www.ungloablcompact.org/ (accessed 23. Feb. 2019).
[24] Human Rights resolution 2003/16, U. N. Doc. CN.4/Sub.2/2003/L. 11 at 52 (2003).
[25] See L. Catá Backer, 'Multinational Corporations, Transnational Law: The United Nations' Norms on the Responsibilities of Transnational Corporations as Harbinger of Corporate Responsibility in International Law' Colum. Hum. Rts. L. Rev. Vol. 37 2005, 101-92.

'protect, respect and remedy' approach.[26] This meant that states are expected to protect human rights, businesses are expected to 'respect' human rights and greater judicial and non-judicial remedies should be made available for the victims of human rights violations resulting from business activities. Since then there has been much work which has sought to clarify how businesses can 'respect' human rights and this has gradually had some influence on business practice.[27] Rather than seeking to modify directors' duties intrinsically or any other aspect of the legal construct of the company, Ruggie's approach was to develop a sense of international responsibility that all businesses should abide by.

Another example of an international organisation taking steps are the initiatives developed by the Organisation of Economic Cooperation and Development (OECD) which has developed guidelines addressed to governments that multinationals should comply with.[28] These are non-binding principles relating to business conduct that provide a multilateral code to which governments agree businesses should comply. However these too are non-binding and do not have any intrinsic impact upon the law within individual jurisdictions relating to the core components of the legal construct of the corporation.

These types of initiatives provide opportunities for companies to comply with non-legally binding standards and as such can be categorised as 'reputational initiatives', as they rely on commercial awareness to ensure that businesses maintain sound reputations in the market place. This can and does mean in practice, that where there is no relevant national law, and where the reputational damage of failing to address an ESG concern is less commercially onerous than the cost of taking the appropriate action, boards of directors may not be easily persuaded to make the financial investment. Therefore the impact of international initiatives of the type mentioned above means that the severity of the reputational, and hence the commercial risk, for the business can determine the extent to which they are taken into account by directors.

3.2 Legislation and Regulation

Interventions with ostensibly more direct influence have come in the form of a variety of types of legislation and regulation. For example some jurisdictions do require increased reporting from companies relating to the decisions that they have taken relating to ESG issues. The EU has introduced the Non-Financial and Diversity Disclosure Directive that requires large companies to publish information related to ESG issues.[29] Similarly in the United States at the Federal level, the Dodd Frank Act requires companies purchasing certain minerals to

[26] United Nations Human Rights Council, *Promotion and Protection of all Human rights, Civil, Political, Economic, Social and Cultural Rights, including the Right to Development,* U.N. Doc. A/HRC/17/31 (2011).
[27] J. G. Ruggie, *Just Business,* (New York: W.W. Norton & Co.) 2013.
[28] OECD, 'OECD Guidelines for Multinational Enterprises (2011). http://mneguidelines.oecd.org/guidelines/ (accessed: 23rd Feb. 2019); see also Principles of Responsible Investment (UNPRI) www.unpri.org (accessed 23rd Feb. 2019).
[29] Directive 2014/95/EU of 22 October 2014.

conduct 'due diligence' investigations relating to their source to ensure that they are not procuring 'conflict minerals'.[30] Such initiatives can be categorised as 'legal compliance initiatives' as they place mandatory obligations upon the operations of companies but do not affect the core legal construct of the company itself.

As has been mentioned, steps to actually amend the nature of directors' duties themselves have been taken place in certain jurisdictions. The United Kingdom was the first to make such a move through its Companies Act 2006 which requires company directors to take certain ESG considerations into account in their decision-making.[31] In other jurisdictions such as Canada, the courts have determined that boards of directors can take into account the interests of other stakeholders that may be relevant to the success of the company. In the case of BCE Inc v 1976 Debentureholders [2008][32] the Supreme Court confirmed that the fiduciary duty of loyalty is owed to the company but that in considering the 'best interests', the board may need to consider the interests of other stakeholders to achieve good business decisions. More recently the French government has been considering amending its civil code to include a 'purpose' for companies that incorporates a responsibility to take into account the environmental and social impacts of their activities.[33] If that legislation is passed, it will take time for its true influence and scope to fully emerge. These types of interventions do provide evidence that 'stakeholder theory' or the more nuanced Enhanced Shareholder Value (ESV) approach is, to a certain degree at least, given leverage within numerous legal systems even if it has not yet materialised as a driving force for decision-making in practice.[34]

These types of developments that can be categorised as 'legal construct initiatives' as they have an impact on the actual fiduciary duties that company directors have. However, in a jurisdiction such as India where corporate law, ostensibly at least gives the appearance of ranking other stakeholders with the same level of importance as that of shareholders,[35] there is evidence directors still make decisions that place commercial interests above those of environmental and social issues.[36] This article argues that these types of drafting adjustments to directors' duties do not affect the overall role that directors' duties [37] play within the broader legal construct of the company, which is designed to attract and maintain investment for commercial purposes. It is also pertinent to note that no jurisdiction has sought to legislate in a manner that would affect the other two components of the legal construct of the company i.e. 'separate legal personality' and 'limited liability'.

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[30] The Dodd Frank Wall Street Reform and Consumer Protection Act (Pub. L. 111-203).
[31] Companies Act s. 172(1)(d).
[32] 3 S.C.R 550.
[33] The proposed PACTE law ('Plan d'action pour la croissance et la transformation des enterprises') would amend article 1833 of the Civil Code to require all companies to include concern of environmental and social impacts in their purposes.
[34] See Freeman (n 19); Stoney & Winstanley (n 19) 603; Andriof et. al (n 19); Keay (n 19) 249-300.
[35] Companies Act 2013 s. 166(2).
[36] Naniwadekar & Varottill (n 17) 95-120.

3.3 Non-Governmental Organisations' Interventions

Finally the interventions of non-state actors need to be considered as they represent a significant proportion of the work that has been carried out in this sphere to date. One of the main influences that non-governmental organisations (NGO) have had is to publicise the operations of companies that have been prejudicial to ESG interests. However, there also non-state actors whose work has sought to create frameworks, guidelines, codes and standards for businesses to comply with. The Forest Stewardship Council (FSC) is an example; it is a multi-stakeholder initiative that has developed voluntary standards that businesses dealing in timber can comply with to obtain certification that grants them market access to those customers that exclude purchases from non-participants of the scheme.[38] This type of incentive for a business is very much 'a reputational initiative' that ties in directly with market access, although motivation for adopting FSC standards can vary.

However probably more prominently in this context NGOs and companies themselves have developed ESG reporting schemes.[39] The proliferation of such schemes has highlighted the work that companies are doing to respond to ESG concerns. Additionally certain stock exchanges have created indices and listings for companies that comply with specific ESG criteria. Notably, none of these interventions by NGOs have a direct impact on directors' duties or the broader legal construct of the company. Therefore they can be classified as 'reputational initiatives' that seek to create commercial pressure on directors by developing greater awareness for investors, customers and employees of the performance of a company *vis à vis* ESG issues.

4. Analysis of the Effect of ESG Initiatives on the Fiduciary Duties of Corporate Decision-Makers.

This section provides an analysis of business decision-making in practice to investigate any 'upper limit' in influence that ESG initiatives may have. This is done by considering decision-making that involves the interface between ESG interests and the constraints that directors face due to their fiduciary duties and the overall legal construct of the company. To carry out this analysis, a series of semi-structured interviews with 18 different heads of corporate responsibility from 15 companies was undertaken.[40] All of the interviews were anonymous

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[38] Forest Stewardship Council, https://ic.fsc.org (accessed: 23rd Feb. 2019); see G. Auld, *Constructing Private Governance: The Rise and Evolution of Forest, Coffee, and Fisheries Certification,* (New Haven: Yale University Press, 2014) 2.

[39] See e.g., The Global Reporting Initiative. https://www.globalreporting.org (accessed: 23rd Feb. 2019).

[40] Interviews undertaken between 8th November 2017 and 29th April 2018. All interview recordings are held on file with the author. The term 'head of corporate responsibility' is used generically. In once case the individual was a CEO. All of the participants took overall responsibility for the management of ESG concerns within their respective companies. The

which meant that interviewees could speak freely and express personal views where appropriate.

The interview analysis is separated into two categories which relate to 'general business strategies' on the one hand and 'investment decision making' on the other. Analysis in the first category of 'general business strategies' relates to the ESG decision-making of the large majority of businesses, in other words those involved in the production, supply and delivery of a wide range of products, resources and services. Therefore the analysis considers how those companies make decisions relating to the impacts that their businesses can have on ESG issues. Analysis in the second category of 'investment decision making' relates to companies that have an entirely different relationship with ESG interests as they need to make assessments of the ESG performance of the companies that they are considering investing in, or which they already hold as investments.

However, within all of the decision-making that is surveyed, the analysis draws from the responses to understand whether there is an upper limit to the extent that ESG initiatives can influence board level decision-making.

4.1 General Business Strategies

In the responses that were given by the interviewees certain key themes recurred. The was a stated willingness of directors to seek to understand the concerns of a range of different stakeholders. However, tied to this willingness was a concern related to the potential commercial impact of failing to do so. For example Interviewee 4 explained that ESG concerns play a part in his company's approach to maintaining support from a spectrum of stakeholders that his business relies on to be successful,

> I have to have the support of the people I deal with and if I have their support I will continue to be in existence, so therefore I need to identify who the people are that I deal with, who our stakeholders are, and our stakeholders really broadly fit into four buckets.[41]

He went on to explain that those four buckets related to customers, communities, employees and partners and that taking their concerns seriously involved the integral and careful management of ESG considerations such as labour standards, environmental protection and proper consultation with communities.[42]

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companies themselves, with the exception of two of the asset management companies, were at the time of the interviews, listed on sustainability indices of either the Dow Jones or FTSE stock exchanges. Of the two asset management companies, each managed in excess of 200bn USD worth of assets worldwide. The companies came from a variety of sectors including banking, insurance, asset management, retail, aerospace engineering, information technology, pharmaceuticals, mineral extraction and food manufacturing.

[41] Interview 007. London (UK). 8th December 2017.

[42] Ibid; see academic arguments for such an approach e.g. Elizabeth C. Kuruz et al. 'The Business Case for Corporate Social Responsibility' in Andrew Crane et. al. *The Oxford Handbook of Corporate Social Responsibility* (OUP, 2008) 83, 86.

It is clear that for many companies that are highly visible to the public, a good reputation with certain stakeholders *vis à vis* ESG factors can be an important component in their commercial success. However this response corresponds to classical critique of stakeholder theory, that the ultimate goal for the business is commercial success and that ESG concerns need to be managed in a way that enable that goal to be realised.[43] Interviewee 17 from a data technology company gave a similar response in terms of the effect that ESG performance can have upon the recruitment of employees. She stated that,

> Another challenge is about the transition that we've made, increasingly being a technology company, as many companies are in a competition, I would say a war for talent, we need to make sure that we are competitive as a good place to work.[44]

The challenge of viability and approval of the various stakeholders ties in with an overall theme which certain interviewees termed as their 'licence to operate'. It was clear that many companies especially those with highly visible reputations such as banks and food manufacturing companies need to maintain a certain degree of approval from the public and those that they deal with in order to continue to be commercially successful. Interviewee 14 stated that, 'what we are trying to achieve in the sustainability universe, is to maintain the bank's social licence to operate'.[45] This was reiterated by interviewee 16 who said that, 'you could bundle all of this under licence to operate. Any large company that wants to be credible needs to be following the frameworks and ideally beating them and having a positive regard to the disclosure of information about ESG risks and opportunities.'[46] The terminology of a 'licence to operate' corresponds longheld with theories relating to 'legitimacy'[47] and 'social contract'[48] that overlap with interpretations of the application of the stakeholder theory in practice and emphasise the need for companies to ensure that they manage commercial risks that have the potential to undermine their position in the marketplace.[49]

Whilst clearly satisfying the expectation of important stakeholders and maintaining a licence to operate are sound commercial practice for the success of a company, the difficulty in strategic decision-making can arise where there is a conflict or a tension between satisfying ESG concerns and the financial cost of doing so. This particular theme was interesting as it demonstrated that companies find certain decisions relating to ESG issues much easier than others and inevitably commercial factors play an important part. In certain instances,

[43] Roby Gray, Reza Kouhy and Simon Lavers, 'Corporate Social and Environmental Reporting: A Review of the Literature and a Longitudinal Study of UK Reporting' (1995) 8(2) 47-77, 53.
[44] Interview 017. London (UK). 31st January 2018; See also Bode, C., Singh, J., and Rogan, M. (2015). Corporate social initiatives and employee retention. Organization Science, 26(6): 1702–1720.
[45] Interview 014. London (UK). 10th January 2018.
[46] Interview 016. London (UK) 30th January 2018.
[47] Craig Deegan, *Financial Accounting Theory* (McGraw Hill, 2014) 343-72.
[48] Ibid 344-7.
[49] Craig Deegan, 'Introduction: The Legitimacy Effect of Social and Environmental Disclosures – A Theoretical Foundation' (2002) 15(3) Accounting, Auditing and Accountability Journal 282-311, 292-5.

such as in the reduction of carbon emissions, companies have been able to rationalise investment in the short term to satisfy longer term commercial gain. For example Interviewee 15 stated that,

> with CO2 emissions particularly for manufacturing it is pretty easy right, we are reducing our direct CO2 emissions from manufacturing quite rapidly ….. you give off less CO2, you use less energy, you cut your costs, it pays back.[50]

In this scenario, persuading a board of directors to follow a policy is helped where there is commercial benefit, at least in the long term. For example in the mineral extraction sector where high volumes of energy and water are often required, there can be significant cost implications involved in reducing that usage. As Interviewee 12 stated,

> there are costs associated with good ESG performance that's certainly true. But I think the trick in the private sector at least, is to try to find where there is an alignment between what the world might generally want, as expressed for example through the SDGs, and what's good for our business.[51]

This indicates an upper threshold in the extent to which ESG initiatives will be supported by boards of directors, that is tied inextricably to the commercial impact and performance of the measure concerned.[52] This trend is consistent with research carried out by Fernando, Sharfman and Uysal of firms in the United States.[53] They examined the different types of approaches that firms take to ESG issues and classified them in two categories. The first related to actions that mitigated ESG outcomes that would ultimately expose the company to commercial risk which they labelled as 'toxicity'.[54] The second related to actions that may have enhanced the company's reputation, and gone beyond what was legally required and management of any conceivable commercial risks, which they labelled as 'greenness'.[55] Their analysis demonstrated that those companies whose approach to managing ESG risks was to avoid commercial 'toxicity' attracted more institutional investment than those firms that adopted 'green policies'.[56] This provides an insight into the approaches taken by institutional investors but also demonstrates that directors of companies are under pressure to manage ESG risks with strategies that are beneficial commercially. It also emphasises the different approaches that firms can take to ESG issues. Rather than being a factor that polarises companies between those that act responsibly *vis à vis* ESG issues and those that don't, the evidence shows that corporate

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[50] Interview 015. London (UK). 11th January 2018.
[51] Interview 012. Johannesburg (South Africa) 21st December 2018.
[52] David Vogel, 'Is there a Market for Virtue? The Business Case for Corporate Social Responsibility' (2005) Cal. Mgmt. Rev. 19, 29.
[53] Chitru. S. Fernando, Mark P. Sharfman and Valnap B. Uysal, 'Corporate Environmental Policy and Shareholder Value: Following the Smart Money' (2017) 52(5) Journal of Financial and Quantitative Analysis 2023-2051.
[54] Ibid 2024
[55] Ibid
[56] Ibid 2045.

decision-making in this regard is more complex, and that the materiality of ESG issues are often recognised as issues that require meticulous financial risk calibration.[57]

Whilst this upper threshold for the acceptance of ESG measures by boards of directors ultimately becomes an issue of commercial judgment, its presence was indicated very clearly by interviewee 2 who stated that, 'if we come in with a wonderful idea and that's going to reduce our profit by X per cent, that will be a hard pitch.'[58] This commercial influence in ESG related risks, is illustrated further by those issues that are particularly difficult to solve. An example of an ESG issue that is particularly challenging is palm oil consumption. Whilst the production of palm oil is not intrinsically harmful in itself, it has been associated with a number of negative environmental impacts including deforestation and habitat loss.[59] Those issues are further complicated by the political and economic pressures related to development and the sovereignty of the producing state. Such issues can be challenging for individual companies to engage with when palm oil is sold as a commodity and sourced from a large numbers of suppliers, rather than from individual plantations.

This leaves a dilemma for those businesses that are engaged in the use of palm oil as an integral part of their business. Interviewee 15 stated that, 'for the commoditised raw materials something like palm oil or sugar, they might be bought many times, aggregated, all of those things and they are traded like oil.'[60] Therefore doing the right thing from an ESG perspective becomes more challenging unless palm oil is eradicated as a component resource within the products that the business is producing. In this instance the industry may attempt to take steps in accordance with certain ESG initiatives, however the demand for related products and the willingness of investors to reap the benefits of such business mean that decisions related to a company's involvement in the procurement of palm oil will ultimately be heavily influenced by commercial factors and these can outweigh the potentially very high cost of introducing effective mechanisms to ensure that those resources are purchased from sources that all have high environmental and human rights standards.[61]

In terms of the fiduciary duties that directors have, such conduct is consistent with decision-making that is being made in the 'best interest of the company' in the traditional sense that it corresponds with decision-making that is ultimately looking to maximise the profit for the shareholder and the company as a whole. Therefore this supports the argument that there is a clear upper commercial limit that restrains the ESG related measures that companies will take. However, a prominent factor evidenced from those companies surveyed was that they are

[57] Ibid
[58] Interview 002, Munich (Germany). 17th November 2017.
[59] See for example, Elsa M. Ordway, Rosamond L. Naylor, Raymond N. Nkongo, Eric F. Lambin, 'Oil Palm Expansion in Cameroon: Insights into Sustainability Opportunities and challenges in Africa' (2017) 47 Global Environmental Change, 190-200.
[60] Interview 015 (n 45).
[61] Nick Pelosi and Rebecca Adamson, 'Managing the 'S' in ESG: The Case of Indigenous Peoples and Extractive Industries' Journal of Applied Corporate Finance (2016) 28(2) Journal of Applied Corporate Finance 87-95.

looking to the interests of the company in the 'long term' as ESG risks can have long lead times.

The 'long-term' understanding of ESG risks and opportunities was one that many interviewees echoed. Interviewee 8 from the property development sector explained that for them,

> 'its about future proofing the business so its about being the developer of choice so that a local authority thinks, I want it to be X company that does that development in my area. So by demonstrating that we can positively respond to challenges like climate change or on the social side to community issues it positions the brand and business very well.'[62]

For interviewee 11 from the mineral and mining sector, made the link between ESG risk and commercial success in the long term was made more explicitly by stating that, 'certainly in the longer term good ESG performance is required for profitability.'[63] In both instances the decision-making carried out at board level with regard to ESG issues was one of 'materiality' or 'financial risk' rather than adopting policies that are sympathetic towards ESG issues purely for their own sake. These responses are consistent with the analysis of Fernando, Sharfman and Uysal.[64] and reflect the influence that investors have in board level strategies.[65] This leads to the next section which looks more closely at the way that asset managers consider ESG issues in the context of the companies that they invest in.

4.3 Investment Decision-Making

The priorities of company directors' emphasis on commercial performance is also seen in the relationship between directors' fiduciary duties and ESG performance in companies involved in making investments and asset management.[66] The competition in the asset management industry to yield the best possible financial returns for clients is a significant driver in decision-making. For example interviewee 001 stated that as an asset manager it was his clients that were the key influence in the manner in which he integrated ESG concerns into the development of asset portfolios not ESG concerns for their own sake. He stated that, 'our role is to provide solutions to client's needs so that is the key driver bar nothing, it is interest and demand.'[67]

What this means in practice is that the extent to which ESG concerns will be integrated into the decisions relating to which companies to invest in, will to a

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[62] Interview 8, London (UK), 8th December 2017.
[63] Interview 11, Johannesburg (South Africa), 21st December 2017.
[64] Fernando, Sharfman & Uysal (n 58) 2045.
[65] Liliana Eva Donath, Roxana Loan and Tatenda Mandimutsira, 'Evaluating the Performance of Socially Responsible Investment Funds' (2018) 65(2) Scientific Annals of Economics and Business 139-58, 154-8.
[66] See Susan N. Gary, 'Values and Value: University Endowments, Fiduciary Duties, and ESG Investing' (2106) 42 J. C. & U. L. 247; for fiduciary duties generally: D. Gordon Smith and Andrew S. Gold (Eds) *Research Handbook on Fiduciary Law* (Edward Elgar, 2018).
[67] Interview 001. London (United Kingdom) 8th November 2017.

large extent be determined by clients rather than by asset managers themselves. As interviewee 1 stated, 'the point of investments in the capital markets is to generate a return to meet whatever liabilities commitments or obligations or mission they have elsewhere.'[68] This is not to say that there is no socially responsible investment (SRI),[69] however it was clear from the interviews undertaken that at this time it remains a limited proportion of overall investment.[70] Interviewee 3 another asset manager, illustrated this by explaining the types of industries that certain clients will exclude from their investment portfolios, 'tobacco is the most common, tobacco, arms, gambling, and we are seeing more carbon related interest as well in terms of carbon exclusions, they are usually around sub-technologies, energy products such as thermal, coal and tar sands rather than carbon more generally.'[71]

Interviewee 6 whose company invested its own funds as well as those of others put it like this,

> we have never really believed in exclusions, to say that we are not going to invest in certain industries and certain companies, but we have such an exclusion for banned weapons and anti-personnel land mines because that is a business that should not be in existence, there's no good in that business, similarly we made a decision to exclude coal in terms of the investment and underwriting of thermal coal companies.'[72]

Evidence suggests that some investors will seek to develop their portfolios excluding specific industries, however that influence is still quite limited.[73]

Research by Duuren, Plantinga and Scholtens, specifically considered the way that asset managers made decisions relating to ESG issues for conventional investment funds (non SRI funds).[74] Their findings support the conclusion drawn from the interviewees in this study that ESG information for conventional investment funds, is being used to manage commercial risk.[75] They state that, 'we find that ESG information in particular is being used for red flagging and to manage risk. We find that many conventional fund managers have already adopted features of responsible investing in the investment process.'[76]

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[68] Ibid

[69] The term 'Socially Responsible Investment' has been given various definitions. See for example: Eurosif, 'European SRI Study 2018' Available at: https://www2.deloitte.com/content/dam/Deloitte/lu/Documents/sustainable-dev/lu-european-sri-study-2018.pdf (Accessed 9th April 2019).

[70] See Hong, H., & Kacperczyk, M. (2009) 93 'The Price of Sin: The Effect of Social Norms on Markets', Journal of Financial Economics' 93, 15–36; Thomas C. Berry and Joan C. Junkus, *Socially Responsible Investing: An Investor Perspective,* (2013) 112, J. Bus. Ethics 707-20.

[71] Interview 003. Edinburgh (United Kingdom) 22nd November 2017.

[72] Interview 006. Zurich (Switzerland) 1st December 2017.

[73] Donath, Loan & Mandimutsira (n 65) 154.

[74] Emiel van Duuren, Auke Plantinga and Bert Scholtens, 'ESG Integration and the Investment Management Process: Fundamental Investing Reinvented' (2016) 138 J. Bus. Ethics 525–533

[75] Ibid 525.

[76] Ibid

A good example of an ESG risk that also represents a commercial risk is that of fossil fuels as coal-fired power stations are on the decline and therefore associated investments can represent long-term commercial risks. As interviewee 2 stated, 'coal is on the decline in the long term economically, therefore they can reduce investments in it. Therefore the two interests coincide.'[77] In 2015 a report partly funded by the United Nations Environment Programme strongly advocated that asset managers should integrate ESG concerns into their analysis of their investments and that,

> fiduciary duties have played and continue to play, a critical role in ensuring that fiduciaries are loyal to their beneficiaries and carry out their duties in a prudent manner. However, we conclude that action is needed to modernise definitions and interpretations of the fiduciary duty in a way that ensures these duties are relevant to 21st century investors.[78]

The report goes on to advocate that greater consideration should be given by asset managers to ESG issues.[79]

However the evidence from this research has demonstrated that for asset managers, normal business practice is to consider the commercial implications of any investment and if ESG issues have a part to play in that process, they should be taken into consideration. As interviewee 3 explained, 'that's not to say that we are amoral but the challenge for my team is for our clients and they are often large clients who have already had the ethical debate and therefore for my team to impose our own ethical values can be a bit of a stretch.'[80]

As such an asset manager will not necessarily avoid the inclusion of companies that have poor ESG performance unless that ESG factor represents a material commercial risk to the investor. Interviewee 3, explained that,

> I think its fair to say that for an unrestricted mainstream equity fund where the mandate is to do as well as you can for that client, the ultimate decision is about the investment outlook. The longer the term of your investment, the more likely it is that ESG will be a factor, but it will be considered as more of a headwind than an existential challenge, and we might still choose to hold that company.[81]

Therefore the concern for ESG issues is affecting the way that investment decisions are being made, but there is clearly an 'upper limit' in the effectiveness of that influence which is dictated to a very large extent by commercial

[77] Interview 002 (n 58).
[78] Rory Sullivan, Will Martindale, Elodie Feller and Anna Bordon, 'Fiduciary Duty in the 21st Century' (United Nations Global Compact, UNEP Finance Initiative, Principles for Responsible Investment and Inquiry: Design of a Sustainable Financial System, 2015) 9.
[79] Ibid at 10.
[80] Interview 003 (n 71).
[81] Ibid.

considerations.[82] As Interviewee 9 put it, 'ES and G, is not about morals its about the actual risks and opportunities to a particular business.'[83]

There is another factor that needs to mentioned and this is the role that asset management companies undertake in 'stewardship' of the investments that they hold.[84] Where asset managers do raise concerns or request information from companies that they hold relating to aspects of ESG performance, it can influence associated decision-making. Naturally companies can be responsive as the asset managers can potentially withdraw holdings. Whilst the influence of this type of 'stewardship' is growing, it is currently only having a limited overall effect on the ESG performance of companies.

In sum therefore, current practice sees asset managers considering ESG risks, but within an overall process of commercial risk management.

5. How can the analysis inform approaches to the protection of ESG interests.

Whatever arguments exist as to the obligations that directors and as a consequence companies *should* owe to ESG issues,[85] the analysis shows that companies naturally prioritise commercial performance. This is consistent with the argument that the duty to 'act in the best interests of the company' functions as an essential component in the tripartite legal construct (including 'separate legal personality' and 'limited liability') that is oriented towards protecting the commercial interests of investors. However what the analysis has also shown is that pressure from ESG initiatives has irrevocably altered the range of factors that companies now need to take into account when they make commercial decisions that can be considered to be in the 'best interests of a company'.[86] This is because a company's performance *vis à vis* ESG issues can have commercial impacts that are related to a company's reputation, legitimacy, its licence to operate (or social contract) and other factors such as its ability to attract good quality employees.

The evidence demonstrates that company directors will only allow ESG factors to influence their decision-making to the extent that they have the potential to have an effect on the commercial success of the business. It shows that where it is possible for a company to make decisions which have positive outcomes for ESG

[82] Bob Herz and Jean Rogers, 'Measuring What Matters: Industry Specificity Helps Companies and Investors Gain Traction on Sustainability' (2016) 28(2) J. Applied Corp. Finance 34-8.
[83] Interview 009. Edinburgh (United Kingdom) 11th December 2017.
[84]See Alice Klettner, 'Chartered Secretary: Stewardship Codes and Shareholder Participation in Governance' (2018) 70(5) Governance Directions 227-234.
[85] See John Edward Parkinson, *Corporate Power and Responsibility: Issues in the Theory of Company Law* (n 20) 304ff; S.H. Goo & Désiree Klingler, 'The Limits of Directors' Duties in Fostering Corporate Social Responsibility and the idea of a Multi-Stakeholder Board' in Paolini (n 1) 194; also Lynn Stout, *The Shareholder Value Myth* (San Francisco: Berrett Koehler Publishers Inc., 2012)
[86] See for example: KPMG, 'ESG Strategy and the Long View – A Framework for Board Oversight' (KPMG, 2017) Available at: https://assets.kpmg/content/dam/kpmg/lu/pdf/lu-en-esg-strategy-framework-for-board-oversight.pdf accessed 23rd Feb. 2019.

issues without incurring significant overheads, boards are easily persuaded. However where there may be a conflict between non-mandatory ESG initiatives and the need to perform commercially, boards of directors are less easily convinced.

This approach is consistent with the guidance of regulators in some jurisdictions who have been required to indicate the proper interpretation of fiduciary duties relating to ESG risks. For example in the United States the Department of Labor issued guidance in 2015 that environmental, social and governance issues "are proper components of the fiduciary's primary analysis,...so long as the investment is economically equivalent, with respect to return and risk to beneficiaries of the economic merits of competing investment choices."[87]

This suggests that the effectiveness of non-mandatory ESG initiatives, exist within a paradigm that is ultimately subject to the vagaries of the market. Those limitations on the manner in which governance relating to ESG concerns is currently designed should inform the manner in which ESG initiatives are designed in the future. For the purpose of this discussion, interventions have been grouped into three categories 'reputational initiatives' 'legal compliance initiatives' and 'legal construct initiatives'. The question in terms of government and governance, is what blend of these types of interventions can be the most effective in achieving effective ESG performance without hampering business and investment.

With regard to 'legal construct initiatives' requiring the re-design of aspects of the traditional legal construct of the company itself, attempts to do so have already occurred and are still occurring in some jurisdictions.[88] Whilst certain states have experimented very tentatively with this approach, lessons from the past demonstrate that individual countries will ultimately be unwilling to adopt law that places those businesses incorporated under their jurisdiction at a competitive disadvantage.[89] Therefore if significant steps in this regard are to take place it would require a high degree of international consensus. (It must of course be noted that there are currently efforts being made at the international level to develop a treaty, that if progressed and adopted, would have the effect of making corporations and other business entities more clearly accountable to international human rights law.[90] Whilst such an initiative would definitely be beneficial, especially in terms of creating greater clarity relating to due diligence and liability,[91] it would not change the legal construct of the corporation itself,

[87] The US Government, Department of Labor, 'Interpretive Bulletin Relating to Fiduciary Standard under ERISA in Considering Economically Targeted Investments' Employee Benefits Security Administration, 29 CFR Part 2509, RIN 1210-AB73, 26 October 2015.

[88] See eg. UK Companies Act, (n 31); also the proposed PACTE law in France (n 33)

[89] See eg Henn & Alexander (n 11) 25.

[90] See UN HRC Resolution. 'Elaboration of an International Legally Binding Instrument on Transnational Corporations and other business Enterprises with respect to Human Rights' UN Doc. A/HRC/Res/26/9 (14th July 2014).

[91] See OHCHR, Open Ended Intergovernmental Working Group on Transnational Corporations (OEWIG), ('Zero Draft') 'Legally Binding Instrument to Regulate in International Human Rights Law, the Activities of Transnational Corporations and Other Business Enterprises' 16th July 2018. Available at:

which would still be pre-disposed to decision-making of the manner discussed in section 2.)

However, what this analysis suggests is that consideration of an entire re-appraisal of the design of the corporation as a legal construct is a crucial exercise that needs to be undertaken. Sjafjell states that, '[w]hile reforming company law will not solve all the problems, it is a missing piece of the sustainability puzzle that needs to be put in its place. It is also a piece that has tended to be ignored in the debate on how to encourage companies to behave in an environmentally and socially friendly manner.'[92]

In terms of external pressure through 'reputational initiatives' requiring voluntary reporting and certification schemes, the evidence has shown that the different initiatives such as the UN Global Compact, the OECD Guidelines, the GRI, the UNPRI and the sustainability indices, have had a significant impact in changing the decision-making attitudes and approaches of company directors as they have raised the 'materiality' of a whole range of ESG factors in commercial decision-making. However they have extrinsic limitations which are compounded by a lack of consistency and competition between schemes, the lack of clarity or applicability of requirements for different sectors, and the lack of comprehensive uptake or engagement by all companies. Therefore whilst such approaches have certain merit their inherent inadequacies need to be taken into account. It is possible that they represent pioneering stages that are paving the way for more adequate systems or frameworks rather than long term solutions in themselves.

By process of elimination, in the short term at least, we turn to 'legal compliance initiatives'. There is a strong case for closer consideration of the use of law and regulation as an intervention to steer company directors towards decision-making that aligns the operations of companies with more positive ESG outcomes. Traditionally of course the response from business and industry is that law and regulation should be kept to a minimum to ensure that businesses are not constrained by 'red-tape'.[93] This reluctance is also reflected to a large degree by the policies of many governments on the issue.[94] From a theoretical standpoint too, there have been long-standing debates relating to the use of regulation to affect the decision-making of companies.[95] The arguments concern

https://www.ohchr.org/Documents/HRBodies/HRCouncil/WGTransCorp/Session3/DraftLBI.pdf

[92] Beate Sjåfell, 'Regulating for Corporate Sustainability: Why the Public-Private Divide Misses the Point' in Barnali Choudhury and Martin Petriu (eds) *Understanding the Company – Corporate Governance and Theory* (CUP, 2017) 145-64.

[93] Daniel Kinderman, 'The Struggle over the EU Non-Financial Disclosure Directive' 8/2015 WSI-Mitteilungen 613, 613-21,

[94] See for example EU 'Non-Financial Reporting Directive' Directive 2014/95/EU provides in the preamble recital 13. that The European Council, in its conclusions of 24 and 25 March 2011, called for the overall regulatory burden, in particular for small and medium-sized enterprises ('SMEs'), to be reduced.

[95] See for example Craig Deegan (n 47) 64-96;

the merits of government regulation,[96] versus approaches that rely on the markets to incentivise certain conduct through customer demand.[97]

Although the evidence from the interviews is limited as it relates only to a small number and reflected personal rather than corporate opinion, it did produce responses that were counter to those that would be expected from those representing a free-market approach to regulation and governance. Clearly whilst no industry seeks additional work or intervention that can slow down production or the provision of services, quite a number of the interviewees considered that of the different types of intervention, regulation in a variety of different forms can be effective. None of them saw regulation as a panacea *per se*, but the trend in the responses was that where it was used in a targeted and well considered manner, it has the potential to effectively and fairly steer decision-making towards positive outcomes for ESG interests.

For example Interviewee 4 spoke of the need for the government to selectively regulate in relation to certain aspects of ESG concerns.[98] Interviewee 7 discussed the use of regulation to create economic incentives.[99] Interviewee 5 stated that, 'I have a personal inclination towards greater regulation, I am not sure if everyone in my company would agree with me, but particularly at an international level, having consideration to labour standards across different countries, having some kind of regulation and enforcement of it would be good.'[100] Similarly interviewee 10 having commented on the influence of reporting frameworks, discussed the disparity of regulatory standards between certain jurisdictions.[101] Whilst it is outside of the scope of this article to consider the wide range of arguments relating to different types of regulation, the comments provided act as a prompt for a systematic review of the areas within which regulation might provide solutions and an analysis of the types of regulation that would be most appropriate to accomplish them.[102]

6. Conclusion

This article has shown that directors' duties are just one component in a very resilient tripartite legal construct that includes 'separate legal personality' and 'limited liability'. That legal construct has been adopted ubiquitously in the

[96] K. Cooper and G. Keim, 'The Economic Rationale for the Nature and Extent of Corporate Financial Disclosure Regulation: A Critical Assessment' (1983) J. Accounting & Public Policy, 2.
[97] M.C. Jensen and W.H. Meckling, 'Theory of the Firm: Managerial Behaviour, Agency Costs and Ownership Structure' (1976) 3 J. Financial Economics, 305-60.
[98] Interview 004, London (United Kingdom) 24th November 2017.
[99] Interview 007 (n 41).
[100] Interview 005. London (United Kingdom) 24th November 2017.
[101] Interview 10, Gothenburg (Sweden) 19th December 2017.
[102] See also for example, UK Govt. DEFRA, 'Smarter Environmental Regulation Review – Phase 1 Report: Guidance and Information Obligations' (2013) Available at: https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/199868/serr-phase1-130516.pdf (Accessed 10th April 2019); also BuroHappold, 'Help or Hindrance? Environmental Regulations and Competitiveness' (Aldersgate Group, 2017) Available at: http://www.aldersgategroup.org.uk/latest/detail:beyond-red-tape-smart-regulations-are-key-to-delivering-uk-industrial-and-environmental-ambitions (Accessed: 10th April 2019).

corporate law of countries around the world as it has been an effective format for business to attract and maintain investment. The analysis has shown that the tripartite legal construct of the company, is inherently designed to protect the interests of investors and as such plays a commanding influence on the way that corporate decision-makers make decisions. Unfortunately that design is also pre-disposed to producing certain unwanted outcomes relating to ESG issues.

The article has assessed the effectiveness of existing ESG initiatives. It has shown that if ESG policies and strategies cannot be aligned with long-term commercial success, boards of directors will be reluctant to incorporate them. This ultimately means that an 'upper limit' to the effectiveness of non-mandatory ESG initiatives exists. This 'upper limit' requires other types of intervention to be developed. This article has suggested that whilst traditionally the business community will push back against additional law and regulation, it can actually garner support where it is introduced fairly and equitably. This is especially the case for those companies that actively take ESG concerns seriously as part of their business practices.

What this article also demonstrates is that there is a broader long-term case for reconsidering the design of the legal construct of the company itself. The existing design has been extremely successful over the last 220 years in providing a medium for businesses to attract and maintain investment. However, it has been less successful in terms of the impacts that companies have had on peoples' human rights and the environment. The article has demonstrated that a re-design of the corporation as a legal construct requires a process that takes into account all aspects of its key components rather than isolating and solely focussing upon directors' duties. What is also clear is that whatever re-design or new framework might be envisaged for the future, it would need to incorporate mechanisms that would ultimately continue to encourage investors and protect their interests if the corporation is to continue to be successful as a medium for business in free market economies.