



Corporate Purpose and Directors' Duties



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Seminar on Corporate Law, Corporate Governance and a Sustainable Future
8th December 2020

Aim of this short presentation

- ▶ To give an overview of a range of actual and proposed law reforms that rely on corporate purpose and/or directors' duties to steer companies towards taking greater account of sustainability in their decision-making





Corporate Purpose


Three Varieties of Corporate Purpose

- ▶ Reform of the **general purpose** of companies?
 - E.g. ‘pursuit of sustainable value within the planetary boundaries’
- ▶ Requiring or allowing companies to specify an **aspirational purpose** or reason for their existence (along the lines of French loi pacte *raison d’être*)
 - A preliminary managerial commitment to moving towards a legally binding purpose or a(nother) soft law statement aimed at markets?
- ▶ Allowing companies to embed a more **specific purpose** in their constitution/by-laws/articles (along the lines of French *société à mission*)
 - *A legally binding purpose against which the CEO and other executives are evaluated, but also creating a safe harbour against challenges to decisions*


Implementation and enforcement of general purpose

- ▶ Difficult to enforce 'sustainable value within planetary boundaries' directly (BJR, discretion)
 - ▶ Ways of achieving this general purpose should be developed in the company's business model and strategy
 - ▶ Duty of board to oversee continuous development and implementation of business model and strategy, including conduct of ongoing due diligence by management (reporting on how negative impacts and risks are addressed)
 - ▶ Aim is to identify and internalise social and environmental externalities on a continuous basis
 - ▶ Could be supplemented by sustainability accounting that identifies the full costs of corporate activity or by stakeholder ('hybrid') forums in which affected groups and experts meet to identify externalities and solutions to them
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Implementation and enforcement of a company-specific, aspirational *raison d'être*

- ▶ Companies could be required or allowed to do this
 - ▶ In France, it is a public commitment to a purpose beyond shareholder value: steps to achieve it should be set out in the strategy, and in the long-term the strategy should be guided by it.
 - ▶ If the *raison d'être* is included in the articles, it will be the duty of the directors to observe it
 - ▶ In the UK, it is not in the articles and so not enforceable directly, but indirectly by means of market forces; some kind of accounting or reporting on whether the purpose has been achieved is also necessary
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Enforcement of (company-specific) *mission*

- ▶ The *mission* is a **specific** social or environmental challenge included in the articles, and going beyond the *raison d'être*, that the company commits to addressing
 - ▶ Policy aim is not encouraging company to internalise (address) its own externalities (social costs) but creating scope for company management to commit to long-term investment in innovation
 - ▶ Reduction of short-term pressures, but CEO and management held accountable by shareholders for progress in achieving the *mission* ('custodianship model of shareholder engagement')
 - ▶ At the same time, exercises of managerial discretion in pursuit of the purpose could not be challenged, giving more scope to balance non-shareholder interests and make credible commitments
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Directors' duties

Directors' sustainability duties without changes to purpose

- ▶ Changes to purpose not essential to increase relevance of sustainability in corporate governance. For example, regulators could:
 - Require directors to develop, disclose and implement a forward-looking corporate sustainability strategy that 'identifies and addresses material environmental and social issues and significant impacts connected to the company's business model, operations and supply chain.'
 - Deliberate or accidental failure to comply with this obligation (e.g. non-implementation) would be a breach of duty enforceable by shareholders or public authority (where causes loss to stakeholders)
 - Complement duties with requirement to link management incentives to KPIs identified in the sustainability strategy
- ▶ See A. Johnston, J. Veldman et al, 'Corporate Governance for Sustainability'
https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3502101

Directors' sustainability duties with change to general purpose

- ▶ Alternatively, duties could be linked to overarching general purpose of companies (sustainable value within the planetary boundaries)
 - Duty of board to promote this purpose by ensuring business model and strategy achieves it
 - Sustainability assessment and due diligence, with management report on how negative impacts and risks dealt with
 - Compliance a condition of continued registration
 - Public enforcement of company law: reflecting shift in focus of company law towards common good of sustainability
- ▶ See B. Sjøfjell et al, SMART Reform Proposals
<https://ssrn.com/abstract=3595048>

Directors' sustainability duties with company-specific purpose (*mission*)

- ▶ The aim of company-specific purpose is to develop the *raison d'être* by specifying social and environmental objectives in the articles
 - *Loi Pacte* requires *société à mission* to set up a body, containing at least one employee, responsible for monitoring execution of mission and reporting to the board; implementation should be verified by a third party body
 - In French law, the directors are legally bound to manage the company in its own interest, whilst considering the social and environmental impact of its activities (Art 1833, a duty of vigilance); but they are also under a duty to observe the articles and develop a strategy that pursues the goals specified in the mission
 - Directors could be sued by the shareholders for failure to honour the commitment (and other stakeholders might ultimately take legal or other action were public commitments are not honoured)
- ▶ For more information on France, see [Segrestin, Hatchuel and Levillain \(2020\)](#)



Thanks for your attention!