

«Say on Strategy without Responsibility»?



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1. Introduction of recent developments¹

With increased business attention to climate change, investors being more aware of the significant economic effects of climate change and the rise of climate change litigation against companies, members of the board of directors² today face challenges which go beyond their previous duties and obligations. As of 1 January 2022, the new provisions in the Swiss Code of Obligations (CO, art. 964a to 964c CO) stemming directly from the Responsible Business Initiative's indirect counterproposal entered into force, making the non-financial reporting for the business year 2023 mandatory for large companies of public interest.³ The respective Swiss ordinance on climate disclosures will come into effect as of 1 January 2024, giving further guidance to companies on their non-financial reporting.⁴ Additionally, the Swiss Criminal Code (CC) has been amended to include the new provision art. 325^{ter} CC, pursuant to which also board members may be held criminally liable in case the non-financial report contains incorrect facts or statements or omits information that is subject to disclosure.

While the respective Swiss legal framework has so far been rather limited in scope (which can lead to uncertainty rather than freedom of choice for companies), standards in the EU and other foreign jurisdictions are much stricter. Depending on their operations in foreign countries, many Swiss companies will be required to also comply with foreign laws (e.g. EU directives). Furthermore, as various stakeholders (such as investors and NGOs) demand comparable disclosure on non-financial information, Swiss companies are well advised to consider international best practices to address such investors and NGOs expectations.

- 1 For this publication, references up to mid-November 2023 were considered.
- 2 The terms board and board of directors are used interchangeably.
- 3 <<https://www.bj.admin.ch/bj/de/home/aktuell/mm.msg-id-86226.html>> (13 November 2023).
- 4 <<https://www.admin.ch/gov/en/start/documentation/media-releases.msg-id-91859.html>> (13 November 2023).

Whether a company ultimately meets the shareholders' expectations, will also be seen at the companies' annual general meetings in 2024 when the shareholders will vote on the non-financial report in accordance with art. 964c CO for the first time on a mandatory basis. Regardless of the legal or practical consequences a vote against such report may have, such vote will send a clear message to the board and may bear a significant reputational risk for the company as well as for individual board members, and in particular the chairperson.

This article gives a short overview of the ultimate responsibility for the non-financial reporting, the board's challenges in case the report is not approved by the shareholders' meeting as well as touch on potential personal liability the board members need to be aware of.

2. Responsibility for non-financial reporting

According to art. 964c CO, the non-financial report must be approved and signed by the supreme governing or administrative body, i.e. for Swiss stock corporations the board of directors, and approved by the «body that is responsible for the approval of annual financial statements», i.e. for Swiss stock corporations the shareholders' meeting.⁵ While Swiss law does not explicitly state which corporate body ultimately carries the responsibility for the non-financial reporting, we are of the view that this responsibility sits with the board as the sustainability strategy of a company forms part of the board's general responsibility for the company's overall strategy. In practice, the sustainability strategy is regularly sub-delegated to a specific board committee, which may either be exclusively tasked with the sustainability strategy or in combination with other tasks such as governance and/or remuneration. However, such sub-delegation does not alter the board's ultimate responsibility. By separately mentioning the signature requirement of the board in art. 964c para. 1 CO, its personal responsibility is further emphasized. The signatory requirement is, however, rather of a declaratory nature and does not have any further legal effect.⁶

5 Art. 698 para. 2 ciph. 4 CO.

6 See eg.g. BÜHLER CHRISTOPH B., Nichtfinanzielle Berichterstattung nach dem Gegenvorschlag zur Konzernverantwortungsinitiative und ihre Bedeutung für den Finanzsektor, SZW / RSDA 6/2021, p. 723.

The new rules did not introduce a vicarious liability of the Swiss holding company for misstatements of its subsidiaries and controlled suppliers as envisaged with the Responsible Business Initiative.⁷ This initially proposed concept was successfully challenged by the people.

An independent review and assessment of the non-financial report by an external auditor is currently not required by Swiss law. The Federal Department of Justice found such review, if limited to the existence of the report, of minimal value and a material assessment as too burdensome and expensive.⁸ However, in September 2023, the Swiss Federal Council announced its intention to introduce such audit requirement in line with its general ambitions to harmonize Swiss sustainability rules with international benchmarks.⁹ The European CSRD for example already incorporates such requirement.¹⁰

This development is also in line with some proxy advisors' guidance that shareholders should vote against the non-financial report in case the report was not verified by an independent third party.¹¹

3. Shareholders' vote on the non-financial report

3.1 Legal nature of the vote

Art. 964c CO leaves it open whether the shareholder approval on the non-financial report is of binding or of consultative nature.

The separation of powers and duties of the board and the shareholders' meeting are, however, an essential element of a Swiss stock corporation. It finds its basis in the so-called principle of parity (Paritätsprinzip).¹²

7 Bundesbeschluss über die Volksinitiative «Für verantwortungsvolle Unternehmen – zum Schutz von Mensch und Umwelt», BBl 2017 6379.

8 Explanatory report of the Federal Office of Justice on "Transparenz bezüglich nichtfinanzieller Belange und Sorgfaltspflichten und Transparenz bezüglich Mineralien und Metallen aus Konfliktgebieten und Kinderarbeit" of 19 November 2019, p. 17.

9 <<https://www.admin.ch/gov/de/start/dokumentation/medienmitteilungen.msg-id-97782.html>> (13 November 2023)

10 Directive (EU) 2022/2464 of the European Parliament and of the Council of 14 December 2022.

11 Cf. for example Ethos 2023 Proxy Voting Guidelines <https://www.ethosfund.ch/sites/default/files/2022-12/221212_lignes_directrices_de_vote_2023_EN_FINAL.pdf> (13 November 2023).

12 BÖCKLI PETER, Schweizer Aktienrecht, 5. A., Zurich/Geneva 2022, § 8 para. 6.

The respective non-transferable and inalienable duties of both bodies are, therefore, explicitly stated in the CO.¹³ As a consequence, tasks that form part of the non-transferable and inalienable duties of the board must not be delegated to the shareholders' meeting (Kompetenzdelegation), and vice versa, and are with the sole responsibility of the respective corporate body. On the one hand, the board cannot shift its responsibility for those duties to the shareholders' meeting, neither through a decision by the meeting nor through a mere approval (Beschlussdelegation). On the other hand, it is also not possible for the shareholders' meeting to attract such responsibility via a change to the company's articles of association (Kompetenzattraktion) or in a single instance (Kompetenzusurpation).¹⁴ In case the shareholders' meeting votes on a matter that does not fall within its authority, such approval can only be of consultative nature. This also holds true in case the law explicitly requires the shareholders' approval for a certain matter, e.g. art. 964c CO.¹⁵

A shareholder has only one single (financial) obligation which is to pay in the full amount of its share(s) in the company.¹⁶ Conversely, its rights are also limited to the appointment of the corporate bodies, approval of the annual report and resolutions concerning allocation of the profit, which it can vote on at the annual shareholders' meeting (Art. 698 para. 2 CO).¹⁷ Beyond the mentioned obligation and rights, the shareholder should not be further involved in the strategy and management of the company. A shareholder also has no fiduciary duties vis-a-vis the company. Board members, to the contrary, have a list of duties as set out in art. 716a CO; they have a fiduciary duty of care vis-a-vis the company and in case such duty is violated they may become personally liable vis-a-vis shareholders or creditors.¹⁸

Based on the above, deciding on the company's strategy, including the sustainability strategy documented in the non-financial report, belongs in our view to the non-transferable and inalienable duties of the board of directors and cannot be delegated to the shareholders' meeting. It should not result in a limitation of liability for the board. Even an engaged shareholder – specifically of a publicly listed company – would be too remote from the company's actual business activities to be able to properly assess the highly complex content of the non-financial report, and the sustainably strategy of the company in general.

In that sense the vote on the non-financial report is fundamentally different from e.g. the election of board members or the remuneration of the board or the executive management as the latter can be better assessed without detailed information available. It can be argued that these votes are aimed at steering the company in a certain direction.¹⁹ The binding nature of the shareholders' approval of the annual financial report according to art. 698 para. 2 CO is a logical consequence of the shareholders' financial interest in the company. This is by nature not the case for the non-financial report.

Finally, we would like to compare the nature of the vote on the non-financial report with the vote on the compensation report. According to art. 735 para. 3 ciph. 4 of the CO, the remuneration report must be submitted to the general meeting for an advisory (consultative) vote if the variable remuneration is voted on prospectively. Such vote does not directly interfere with the non-transferable and inalienable duties of the board of directors but may give the board a broad hint on the future direction with a view to its upcoming annual re-election.

13 Art. 716a para. 1 CO for the board of directors and art. 698 para. 2 CO for the shareholders' meeting.

14 BÖCKLI (loc.cit.), § 8 para. 46, 48; ISLER MARTINA, Konsultativabstimmung und Genehmigungsvorbehalt zugunsten der Generalversammlung, Diss. Zurich 2010 (= SSHW 297), p. 27.

15 ISLER (loc.cit.), p. 157.

16 Art. 680 para. 1 CO.

17 And for listed companies, to vote on the compensation of the board, advisory board and executive management (art. 698 para. 3 CO).

18 Art. 717 CO.

19 However, the mandatory and binding shareholder vote on the remuneration of the executive management was also highly criticized as the board is in most cases better placed to assess an adequate compensation that meets the expectations of the competitive international labor market and ensures to attract and retain the talents for the success of the company.

Based on the above, we strongly believe that the vote on the non-financial report has to be of consultative nature. The statutorily required vote of the shareholders' meeting should not interfere with the board's non-transferable and inalienable duties and consequently should also not undermine its liability for them.²⁰ To create «a say on strategy without responsibility» cannot be in anyone's interest.

3.2 Consequences in case the shareholders' meeting votes against the non-financial report

Even though we are of the view that the shareholders' vote on the non-financial report is of consultative nature, and therefore the vote is not legally binding for the board²¹, the question remains what the factual consequences/impact are if the shareholders do not approve the non-financial report. Should the company only take note of the shareholders' vote against it or would the company be better advised to bring a revised version of the report to a vote at the next ordinary shareholders' meeting?

The board might be caught between its duties vis-a-vis the shareholders to respect their vote and the legal reporting requirements pursuant to which the board is obliged to inform the public of the company's sustainability efforts and achievements. Since Swiss law does not require an independent audit to date, proxy advisors and investors may deem a vote against the non-financial report as an opportunity to provide feedback on the company's overall sustainability strategy (Signalwirkung).²²

As mentioned above, the board has fiduciary duties vis-a-vis the company, i.e. it has to ensure that the purpose of the company as well as its long-term interests to generate financial profit are respected.

These interests are not necessarily aligned with the interests of the shareholders who do not have any obligations vis-a-vis the company, other than to pay in the full amount of their shares. It may be that shareholders have only short-term interests in the company and therefore want to maximize profits in the near future, to the detriment of a more sustainable strategy and profit.

Consequently, while the board should take criticism of the shareholders on the non-financial report seriously (be it for the company's sustainability strategy or future non-financial reports), we think it would only make sense for the board to bring a more polished version (taking shareholders' criticism into account) of the report to the next ordinary shareholders' meeting in case the board agrees with the shareholders and considers changes necessary or appropriate based on its own assessment. This should especially hold true in cases where the non-financial report was audited. A publication of the non-financial report without taking into consideration any criticism of the shareholders despite the shareholders' vote against it, may bear the risk that the board member(s) will not be re-elected at the next shareholders' meeting or that they will not be discharged.

4. Potential civil and criminal liability of the board members

4.1 Legal basis

Board members of a Swiss stock corporation may become personally liable for the negative consequences of their acts and omissions if certain conditions are fulfilled.²³ The company, its shareholders as well as creditors may have standing to claim damage against board members; the latter however only in case of bankruptcy of the company.²⁴

20 BÖCKLI (loc.cit.), § 8 para. 54.

21 ISLER (loc.cit.), p. 92.

22 Cf. also ISLER (loc.cit.), p. 95.

23 According to art. 754 CO such requirements are: Damage (primarily the damage of the company), violation of duties (in particular the duty of care according to art. 717 CO), adequate causation between damage and the violation of duties, as well as fault (whereby simple negligence is sufficient).

24 Art. 756 and 757 CO.

In case of a bad decision making, the liability of a board member is, however, limited due to the so-called "business judgement" rule: The Swiss Supreme Court acknowledged that a board member has a certain discretion and even if a decision turns out to be wrong at a later point in time it does not lead to a liability if, at the time of the resolution, the board member was not conflicted and had carefully assessed the relevant facts that led to the decision (i.e. ex-ante view).²⁵

Under the newly introduced art. 325ter CC, a board member may also be held criminally liable in case of non-compliance with the new reporting obligations.²⁶ Any violation of the reporting obligations will be prosecuted ex officio.

In addition, board members may be subject to criminal liability in accordance with the provisions that are generally applicable in a business context, such as e.g. mismanagement according to art. 158 CC.

4.2 Potential impact of shareholders' vote on board liability

What consequences may a positive or negative shareholders' vote on the non-financial report have for the board's liability? Does it matter whether the vote is of binding or of consultative nature? In line with our view that the shareholders' approval on the non-financial report is of consultative nature, we focus on what impact such vote may have on the potential board liability.

In case the shareholders approve the non-financial report, the board ultimately receives feedback that it is (according to the majority of shareholders) on the right track with its sustainability strategy which provides a certain level of comfort, in particular, if the approval is paired with shareholders discharging the board for the preceding business year.

However, this does not mean that the board can fully rely on the shareholders' approval as *décharge* is only provided to the extent shareholders know or can reasonably know about the facts that form the basis of the non-financial report, the sustainability strategy and the actions of the board in general.²⁷ Further, should shareholders become aware of a fact that happened in the previous, and for the vote relevant, business year after the shareholders' approval, they would still be entitled to hold the board members responsible under art. 754 CO, or press charges under the relevant criminal provisions. In addition, as mentioned earlier, the board is not only confronted with the demands and expectations of shareholders but also regulators, NGOs, and other interested parties and thus needs to take their interests into account as well.

In case the shareholders disapprove the non-financial report in the declaratory vote, it puts the board of directors into a difficult situation. It may well be that the board does not know the reasons for the negative vote, or it may know about the reasons but not agree with the opinion of the shareholders as either the shareholders lack the necessary insights to come to the «in the view of the board» right decision or they don't take all interests of the company into account. By simply following the criticism of the shareholders' meeting, the board could be exposed to liability claims by creditors, regulators or shareholders who agreed with the board in the first place.

To summarize the above, irrespective of a positive or negative vote by the shareholders, the board needs to make an independent assessment as it ultimately remains responsible for the content and completeness of the non-financial report.²⁸

Would the situation be different if the view was taken that the shareholders' vote is binding? We would think so, as a binding vote by shareholders would ultimately result in a certain limitation of liability of the board. In both scenarios, the ex officio prosecution of the criminal sanctions would however not be touched.

25 Initial decision BGER 4A_74/2012 of 18 June 2012, para. 5.1; further references BÖCKLI (loc.cit.) § 16 para. 257 et seqq.

26 Under this provision, a person shall be liable to a fine not exceeding 100,000 francs if he or she willfully provides false information in the reports in accordance with art. 964a, 964b and 964l CO or fails to make the required reports (including the non-disclosure of information that is subject to disclosure), or if he or she fails to comply with the statutory obligation to retain and document the reports in accordance with art. 964c and 964l CO. A person who acts negligently shall be liable to a fine not exceeding 50,000 francs.

27 Art. 758 para. 1 CO.

28 Cf. also BÖCKLI (loc.cit.), § 8 para. 54.

4.3 Mitigants to be considered for board liability

Potential negative side effects for the board in case of a shareholders' vote against the non-financial report may be that the board member(s) may not be re-elected at the next general meeting in case shareholders disagree with the board's sustainability strategy or their efforts towards sustainability ambitions, or shareholders may as well refuse the *décharge* to the board for this reason. The bigger issues are, however, the reputational damage and the communication efforts (including managing the media) that will be needed to restore the good standing of the company. Finally, a negative vote may also set a trigger point and thus increase the likelihood of litigation by third parties, such as NGOs.

The board thus must think of potential mitigants which should help to strengthen its position vis-a-vis the shareholders and build a line of defense for the board to confront potential reputational or liability risks. One of such potential mitigants – as outlined above – could be the (limited) assurance for the non-financial report by an external auditor on a voluntary basis. Such third-party (limited) assurance from an audit firm can clearly improve the reliability of sustainability information as well as the overall credibility of the disclosure. Further, it is crucial to have an adequate and fit for purpose governance and related processes around sustainability in place. The governance framework should support sound decision-making and allocate clear responsibilities (also to monitor emerging ESG risks) and accountabilities on board level, but also on the levels below the board. It should ensure that sustainability is being considered appropriately at all levels and closely monitored and considered in the same manner as financial topics. Further, ESG expertise and experience on board level is key and can e.g. be gained or improved through regular adequate training of board members.

Ultimately, the board needs to have all tools at hand to take informed decisions (keyword business judgment rule) and to exercise the business judgement and effective oversight in relation to ESG-related commitments throughout the company. With the current pace of ever-changing sustainability regulations and requirements globally, the board needs to be able to count on sound management processes and clear reporting lines.

5. Concluding Remarks

The expansion of board responsibilities to include ESG-topics is currently seen globally and reflected in international standards and domestic regulations. Given the growing consensus around ESG-performance tied to company value, boards have a lot more to consider. As ESG is clearly an important focus area in the boardroom, the board is now challenged to address ESG-related (and potentially diverging) expectations of different stakeholders in a balanced manner.

With the increased pressure of a company's successful implementation and governance of ESG, boards will benefit greatly from continuing education as they carry out their oversight responsibilities. Boards should also consider good ESG-governance as an element of strategic importance to attract customers, investors, and employees or as an opportunity for the company's growth. The boards are therefore challenged to integrate ESG in the structure of the company's organization in a convincing manner. Going way beyond the company's corporate purpose, shareholders expect companies to answer how Corporate Social Responsibility is being considered and what measures are being taken to implement it.²⁹

The shareholder meetings 2024 will give a good indication on how well the board will manage these additional responsibilities and challenges and whether the board has successfully met the shareholders' expectations.

29 SUTTER-RÜDISSEY MICHÈLE / HORBER FELIX, Die Nachhaltigkeit als neues Standbein der Corporate Governance, in: Board Dynamics | Coping with Uncertainty. Actions for the Now and the Future, NICG 2021/1, St. Gallen 2021, p. 45.