

TRENDS IN REGULATORY EXPECTATIONS AND THEIR IMPACT ON COMPLIANCE MANAGEMENT IN COMPANIES

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ABSTRACT

Compliance requirements for companies are growing, especially in the fields of ESG (Environmental, Social, and Corporate Governance) and data privacy. The phenomenon can be observed not only within the EU, but also many other areas of the world. Within the regulatory environment, fostering ESG practices has long since developed from a voluntary commitment to a “real” compliance issue which lawmakers are driving forward with serious sanctions and which courts are also shaping within the framework of the evolving laws. These laws are very complex, often unclear, and intrude deeply into the areas of risk analysis and risk management, which traditionally represent a core responsibility of companies. Many regulations emphasize development and implementation of internal processes within companies. This greatly reduces companies’ discretionary powers, since responsible use of leeway is a core area of entrepreneurial decision-making governed by the business judgment rule. Structurally, we are seeing increased legalization of risks, through which the legislator *de facto* takes away companies’ leeway to make entrepreneurial decisions. Also, the threat of severe fines and uncertainty about the interpretation of legal terms makes it difficult for companies to decide what needs

to be done to meet the laws' requirements and to avoid risk. Looking at the character of the regulations, we see value-driven and symbolically-charged laws. However, these laws are anything but "dead letters" – they intervene deeply in companies' risk management, aim at changing behavior, and have sharp "teeth" in the form of sanctions. The EU may be a particularly fertile source of symbolic legislation, which can serve to create political identity. Companies can, however, choose different ways to deal with these challenges, and they are free to find the right path. Even if lawmakers are increasingly intervening in the way companies carry out risk analyses and the priorities they set in that context, companies should defend their leeway and use it wisely. It is of utmost importance to know the real risks well and to use leeway responsibly. A diligent risk analysis, carefully aligned to a company's circumstances and needs, is always a good starting point. Perfect knowledge of applicable laws and the company's operations is a prerequisite for a professional risk assessment and building an effective Compliance Management System (CMS). There is always room for balanced decision-making regarding risk assessment and prioritization in accordance with the business judgment rule and entrepreneurial responsibility.

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I. INCREASING COMPLIANCE REQUIREMENTS

It has become almost a commonplace to state that compliance requirements for companies are constantly increasing. And yet this is true, and it is all the more remarkable when one looks not only at existing regulations but also at those still in the legislative pipeline. Especially in an international context, it is necessary to examine overarching developments as well as legislative trends and determine whether they have broader significance. This allows companies to prioritize implementation of diverse aspects of compliance management more appropriately.

A. European Union

For the European Union (EU), the following are key areas:

- The concept of “Environmental, Social, and Corporate Governance” (ESG) plays an increasingly important role in the EU's legislative plans
- Data protection and information security continues to be a main focus since implementation of the *EU General Data Protection Regulation* (EU GDPR)

In the area of **ESG**, the European Parliament and EU member states adopted a directive in 2014, entitled the *EU Non-Financial Reporting Directive*, to expand the reporting obligations of large capital market-oriented companies, credit institutions, financial services institutions and insurance companies.¹ With the *CSR Directive Implementation Act* of 2017, which also applies to management reports, e.g. Germany has transposed this directive into national law. Companies are required to disclose information on environmental issues, social issues, treatment of employees, respect for human rights, anti-corruption and anti-bribery efforts, and diversity on company boards in terms of age, gender, educational, and professional background.² With the *EU Corporate Sustainability Reporting Directive*, the *EU Non-Financial Reporting Directive* will now to be extended, beginning in the 2025 financial year, to all companies with more than 250 employees, a balance sheet total of at least 20 million Euro, or annual sales of more than 40 million Euro. From January 2028, even capital market-oriented small and medium-sized enterprises will be added to the list.³ In the event of infringement, fines of up to 50,000 Euro may be imposed, and in the case of capital market-oriented corporations up to two million Euro or twice the economic advantage derived from the infringement, whereby the economic advantage includes estimated profits made and losses avoided.

In September 2020, a report prepared by the European Parliament's Committee on Legal Affairs (JURI) on its own initiative became public. It contained recommendations to the EU Commission for its draft on a supply chain due diligence directive. This resulted in the draft EU Directive on Corporate

¹ European Parliament, *Non-financial Reporting Directive*, Europa.eu (Jul. 19, 2022), [https://www.europarl.europa.eu/Reg-Data/etudes/BRIE/2021/654213/EPRS_BRI\(2021\)654213_EN.pdf](https://www.europarl.europa.eu/Reg-Data/etudes/BRIE/2021/654213/EPRS_BRI(2021)654213_EN.pdf).

² Bundesministerium der Justiz, *Gesetz zur Stärkung der nichtfinanziellen Berichterstattung der Unternehmen in ihren Lage- und Konzernlageberichten*, bmj.de (Sep. 21, 2016), <https://www.bmi.de/SharedDocs/Gesetzgebungsverfahren/DE/CSR-Richtlinie-Umsetzungsgesetz.html>.

³ European Commission, *Corporate sustainability reporting*, Europa.eu (Jul. 19, 2022), https://ec.europa.eu/info/business-economy-euro/company-reporting-and-auditing/company-reporting/corporate-sustainability-reporting_en.

Sustainability Due Diligence (EU CSDD Directive) in 2022. The focus is on sustainability obligations for companies, with the aim of promoting sustainable and responsible corporate behavior in all global value chains.⁴ The core elements of the directive are the identification, termination and prevention of negative human rights and environmental impacts within companies' operations, subsidiaries and value chains. In addition, certain large companies must develop a plan to ensure that their business strategy is consistent with limiting global warming to 1.5 °C, in line with the Paris Agreement. In the event of a breach, companies will be subject to civil liability for damages and financial penalties based on the company's revenues. Further decisions by regulators containing penalties for breaches of the directive's provisions will be made public. However, the exact nature of the sanctions will be left to the member states' discretion.

Within the EU, there are already national laws that address these issues. France introduced the *Loi de Vigilance* in 2017.⁵ It requires large companies to develop a due diligence plan to identify and prevent risks of serious harm to human rights or fundamental freedoms, to the health and safety of people or the environment. The due diligence plan covers the company's operations, its subsidiaries, and activities of subcontractors and suppliers with which it has an established business relationship. Upon request, any person with a legitimate interest may petition a court to order the company to comply with the requirements. In addition, the company is liable for damages in the event of a breach of the due diligence requirements. The Netherlands also adopted a similar regulation in 2019 with the *Wet Zorgplicht Kinderarbeid*.⁶ The law requires companies to check whether there is a risk that child labor has been used in their supply chain. If this is the case, an action plan to combat child labor must be developed. In addition, if this is the case, companies must make a statement, which will be recorded in a public register, about their investigations and the action plan. If no remedial action is taken within six months, companies face heavy fines, in the worst case even ten percent of annual sales. In the event of repeated violations within five years, managing directors must expect criminal consequences, even a prison sentence of up to six months. In 2021, Germany followed suit with the *Act on Corporate Due Diligence Obligations in Supply Chains* (German abbreviation LkSG).⁷ Companies based in Germany with at least 3,000 employees (starting 2024: 1,000 employees) are required to comply with a number of due diligence requirements to ensure human rights and essential environmental protection standards in the supply chain. Companies are required, among other things, to establish appropriate risk management, issue a policy statement and establish a grievance procedure. These due diligence obligations apply not only to the company's own business operations, but also to direct and (albeit within narrower limits than the present EU CSDD) indirect suppliers. Violations can result in fines of up to 5 million Euro, and for companies with annual (group) sales of more than 400 million Euro, fines of up to two percent of average annual sales.

⁴ Presse Release of European Commission, Just and sustainable economy: Commission lays down rules for companies to respect human rights and environment in global value chains (Feb. 23, 2022), https://ec.europa.eu/commission/presscorner/detail/en/ip_22_1145.

⁵ Legifrance, *Loi de Vigilance*, legifrance.gouv.fr (Mar. 27, 2017), https://www.legifrance.gouv.fr/jorf/id/JORFTEXT00003429062_6/.

⁶ Staatsblad van het Koninkrijk der Nederlanden, *Wet Zorgplicht Kinderarbeid*, officieelbekendmakingen.nl (Nov. 13, 2019), <https://zoek.officielebekendmakingen.nl/stb-2019-401.html>.

⁷ Gesetze im Internet, *Lieferkettensorgfaltspflichtengesetz*, (Jul. 23, 2022), <https://www.gesetze-im-internet.de/lksg/LkSG.pdf>.

On October 22, 2020, the European Parliament adopted a legislative resolution with recommendations to the Commission for an EU legal framework to halt and reverse EU-driven global deforestation.⁸ Extraordinarily far-reaching due diligence obligations are envisaged for companies that introduce raw materials covered by the proposal and products derived from them to the market for the first time within the internal market of the EU, or which finance economic operators carrying out these activities. In November 2021, the EU Commission then presented a proposal for a regulation on deforestation-free products. The aim is to protect against illegal deforestation, especially of rainforests, and the associated risks to the rights of indigenous peoples.⁹ Penalties will include, at a minimum, fines proportionate to the environmental damage and the value of the relevant commodities or products, confiscation of the commodities and products from the operator and/or trader, confiscation of revenues gained by the operator and/or trader from a transaction with the commodities and products plus temporary exclusion from public procurement processes.¹⁰

A second focus area of compliance-relevant EU legislation is **data privacy and information security**. EU GDPR¹¹ was a landmark piece of legislation which imposed many new obligations on companies in 2018. In terms of content, it was not so much a matter of tightening up substantive data protection law. What was decisive and very costly for companies were procedural requirements, i.e. how companies must organize themselves to meet the legal requirements, and of course, the threat of sanctions of up to 10% of annual turnover.

After the EU GDPR was implemented, there have been further plans: The EU Data Act,¹² presented by the EU Commission in February 2022, is intended to ensure "fairness in the digital environment," promote a competitive data market, open up opportunities for data-driven innovation, and make data more accessible to all. The proposal includes measures to give users access to the data generated by their connected devices, measures to improve the negotiating power of small and medium-sized enterprises by preventing imbalances in data-sharing contracts, and funding for public authorities to access and use data held by the private sector.¹³

Other regulations are still pending, such as the EU e-Privacy Regulation, which was actually supposed to be developed with the EU GDPR but was then repeatedly delayed. It should mainly regulate the confidentiality of communications, the processing of communications data, and the storage and reading of information on terminal equipment (e.g., cookies).¹⁴ The aim of the regulation is to align the rules

⁸ European Parliament, Resolution of 22 October 2020 with recommendations to the Commission on an EU legal framework to halt and reverse EU-driven global deforestation, Europa.eu (Oct. 22, 2020) https://www.europarl.europa.eu/doceo/document/TA-9-2020-0285_DE.html.

⁹ European Commission, *Questions and Answers on new rules for deforestation-free products*, europa.eu (Nov. 17, 2021), https://ec.europa.eu/commission/presscorner/detail/en/qanda_21_5919.

¹⁰ European Commission, *Proposal for a Regulation on deforestation-free products*, europa.eu (Jul. 23, 2022), https://environment.ec.europa.eu/system/files/2021-11/COM_2021_706_1_EN_ACT_part1_v6.pdf.

¹¹ European Parliament, *EU General Data Protection Regulation*, Europa.eu (Apr. 27, 2016), <https://eur-lex.europa.eu/eli/reg/2016/679/oj>.

¹² European Commission, *Data Act*, Europa.eu (Feb. 23, 2022), <https://digital-strategy.ec.europa.eu/en/library/data-act-proposal-regulation-harmonised-rules-fair-access-and-use-data>.

¹³ Press Release of European Commission, *Data Act: Commission proposes measures for a fair and innovative data economy* (Feb. 23, 2022), https://ec.europa.eu/commission/presscorner/detail/en/ip_22_1113.

¹⁴ European Commission, *ePrivacy Regulation*, Europa.eu (Jul. 19, 2022), <https://digital-strategy.ec.europa.eu/en/policies/eprivacy-regulation>.

on electronic communications with the EU GDPR.¹⁵ The project is current still being negotiated among the European Parliament, the Council of the EU, and the European Commission.¹⁶ It is unclear whether an agreement will be reached this year.

EU regulators and authorities have been making very clear that they intend to defend the privacy of personal data and will not hesitate to actively do so vis-à-vis the corporate world on an international basis. Prominent examples include Google and Facebook, which have been fined a combined record of 210 million Euro by the French data protection authority (CNIL) for making it difficult for users to stop the companies tracking their online activity.¹⁷

B. United States and United Kingdom

In the area of anti-corruption, both the United States, with the *U.S. Foreign Corrupt Practices Act* (FCPA) of 1977, and the United Kingdom, with the *UK Bribery Act* (UKBA) of 2010, are setting the pace for the development of compliance programs, especially for companies operating internationally. Both sets of rules have extraterritorial reach and can apply to foreign companies even if the acts of corruption were not committed in the United States or the United Kingdom. Both laws threaten serious sanctions. Further, both laws go beyond merely general obligation to comply with the law – they establish concrete guidelines for an effective compliance program which companies and their managers must follow if they want to influence the outcome of investigations in their favor.

However, in both the United States and the United Kingdom, the importance of other issues is growing, with a trend toward ESG issues and data protection also in evidence here:

In California, for example, the *California Transparency in Supply Chains Act*¹⁸ has been in effect since January 2012. The law requires certain companies to publicly disclose their efforts to eliminate human trafficking and modern slavery in their operations. Companies fall within the law's scope if they identify themselves as retailers or manufacturers on their tax returns, meet the legal requirements to do business in California, and have annual worldwide gross receipts of more than 100 million USD. The goal is to provide consumers with enough information to make informed purchasing decisions about goods. Consumers should have the choice to buy goods produced by companies that manage their supply chains responsibly, thereby reducing slavery and human trafficking.¹⁹

¹⁵ European Commission, *ePrivacy Regulation*, Europa.eu (Jul. 19, 2022), <https://digital-strategy.ec.europa.eu/en/policies/eprivacy-regulation>.

¹⁶ Statewatch, *EU:e-Privacy*, statewatch (Apr. 20, 2022), <https://www.statewatch.org/news/2022/april/eu-e-privacy-council-proposed-amended-mandate-while-in-negotiations-with-parliament/>.

¹⁷ The Guardian, *France fines Google and Facebook €210m over user tracking*, theguardian.com, (Jul. 23, 2022), <https://www.theguardian.com/technology/2022/jan/06/france-fines-google-and-facebook-210m-over-user-tracking-cookies>.

¹⁸ State of California Department of Justice, *The California Transparency in Supply Chains Act*, State of California Department of Justice (Jul. 23, 2022), https://oag.ca.gov/sites/all/files/agweb/pdfs/cybersafety/sb_657_bill_ch556.pdf.

¹⁹ State of California Department of Justice, *The California Transparency in Supply Chains Act*, State of California Department of Justice (Jul. 19, 2022), <https://oag.ca.gov/SB657>.

On the federal level, the *U.S. Uyghur Forced Labor Prevention Act* of 2021,²⁰ passed in late 2021, bans imports from China's Xinjiang region unless the importer can prove that the goods were produced free of forced labor.

The *Virginia Consumer Data Protection Act* of 2021 is an example from the field of privacy protection which protects Virginia consumers.²¹ The Act grants consumers, among other things, the right to inquire whether a controller is processing their personal information, to receive confirmation if that is the case, to obtain access to personal information provided by the controller if it is being processed, and to have personal information deleted upon request if it was provided by or collected about the consumer.

In California, another data security law, the *California Privacy Rights Act*, is scheduled to come into force on January 1, 2023.²² This will significantly expand and update the existing data protection law under the *California Consumer Privacy Act*.²³ The act is intended to prevent the disclosure of California consumers' confidential information. A new agency, the California Privacy Protection Agency, is also being planned to implement the act. Intentional violations can be punished with fines of up to 7,500 USD per violation.

In the United Kingdom, the *UK Modern Slavery Act* (UKMSA) of 2015 is currently in force. It can also have an extraterritorial effect under similar conditions as those established by the UKBA.²⁴ UKMSA requires companies with an annual receipts of 36 billion GBP or more to publish reports on the risks of modern slavery in their own business.

In October 2021, the British government published a strategy paper entitled "Greening Finance: A roadmap to sustainable investing."²⁵ The aim is to promote sustainable investment and make the financial system more environmentally friendly by (among other things) strengthening sustainability and disclosure obligations.

Another important initiative in the field of privacy and digital services is the draft UK Online Safety Bill,²⁶ which was recently introduced in the British Parliament. The bill contains comprehensive requirements for all providers of digital services operating in the United Kingdom, regardless of whether they are based there or not. Providers fall within its scope if they have numerous users in the United Kingdom. In the event of a breach, websites can be blocked, and fines of up to 18 million GBP or 10% of global receipts. However, the law only affects companies which host user-generated content, i.e.,

²⁰ Government Publishing Office, An act to ensure that goods made with forced labor in the Xinjiang Uyghur Autonomous Region of the People's Republic of China do not enter the United States market, and for other purposes, govinfo.gov (Dec. 23, 2021), <https://www.govinfo.gov/app/details/PLAW-117publ78>.

²¹ Virginia General Assembly, *Consumer Data Protection Act*, virginia.gov (Jul. 19, 2022), <https://law.lis.virginia.gov/vacode/title59.1/chapter53/>.

²² *California Privacy Rights Act of 2020*, ca.gov (Jul. 19, 2022), <https://vig.cdn.sos.ca.gov/2020/general/pdf/top1-prop24.pdf>.

²³ California Legislative Information, *California Consumer Privacy Act*, ca.gov (Jul. 19, 2022), https://leginfo.ca.gov/faces/codes_displayText.xhtml?division=3.&part=4.&lawCode=CIV&title=1.81.5.

²⁴ Secretary of State for the Home Department, *Independent Review of the Modern Slavery Act 2015: Final Report*, gov.uk (Jul. 19, 2022) S. 40, https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/803406/Independent_review_of_the_Modern_Slavery_Act_-_final_report.pdf.

²⁵ Government UK, *Greening Finance*, gov.uk (Jul. 19, 2022), <https://www.gov.uk/government/publications/greening-finance-a-roadmap-to-sustainable-investing>.

²⁶ House of Commons UK, *Online Safety Bill*, parliament.uk (Jul. 14, 2022), <https://bills.parliament.uk/bills/3137>.

which allow users to post own content online or interact with each other. The law also covers search engines, which are subject to tailored obligations aimed at minimizing the display of harmful search results to users.²⁷ The law also covers all websites that provide forums, message boards or user-generated content.

In addition to ESG compliance and data protection, corruption remains a high priority, particularly in the United States. As recently as December 2021, the U.S. government presented a comprehensive strategy to combat corruption.²⁸ This includes, first, better understanding and responding to the transnational dimensions of corruption, elevating anti-corruption as a cross-cutting priority in key ministries and agencies across government, and increasing law enforcement resources and information sharing between intelligence and law enforcement agencies.²⁹

C. Other Countries

In countries outside the EU, the United States and the United Kingdom, the trend of prioritizing ESG issues is, unsurprisingly, less pronounced. A few examples show the point:

Japan has some regulations relating to ESG compliance. Examples include the JP Act on Promotion of Global Warming Countermeasures,³⁰ the JP Act on Promotion of Women's Participation and Advancement in the Workplace,³¹ and the JP Green Bond Guidelines.³² In addition, the JP Corporate Governance Code was updated last year. It recommends that large listed companies disclose information on risks and opportunities related to climate change based on a framework established by the Task Force on Climate-related Financial Disclosures.³³

South Africa adopted a draft SA Green Finance Taxonomy in the middle of last year, responding to the increased importance of ESG compliance in the context of investment.³⁴ The draft identifies a minimum set of assets, projects, and sectors that can be defined as "green" in line with international best practices and national priorities. It is intended to be used by investors, issuers, asset owners and other participants in the financial sector.

India is trying to address ESG issues more intensively. A working group set up by the Indian Ministry of Finance is working on the development of a green taxonomy as part of a larger sustainable finance

²⁷ Department for Digital, Culture, Media & Sport, *Online Safety Bill: factsheet*, gov.uk (Apr. 19, 2022), <https://www.gov.uk/government/publications/online-safety-bill-supporting-documents/online-safety-bill-factsheet>.

²⁸ The White House, Fact Sheet: U.S. Strategy on Countering Corruption, whitehouse.gov (Dec. 6, 2021) <https://www.whitehouse.gov/briefing-room/statements-releases/2021/12/06/fact-sheet-u-s-strategy-on-countering-corruption/>.

²⁹ The White House, Fact Sheet: U.S. Strategy on Countering Corruption, whitehouse.gov (Dec. 6, 2021) <https://www.whitehouse.gov/briefing-room/statements-releases/2021/12/06/fact-sheet-u-s-strategy-on-countering-corruption/>.

³⁰ Act on Promotion of Global Warming Countermeasures, cas.go.jp (Jul. 19, 2022), <https://www.cas.go.jp/jp/sei-saku/hourei/data/APGWC.pdf>.

³¹ The Act on promotion of Women's Participation and Advancement in the Workplace, gender.go.jp (Jul. 19, 2022), https://www.gender.go.jp/english_contents/about_danjo/lbp/pdf/promotion_of_woman.pdf.

³² Japan's Green Bond Guidelines, env.go.jp (Jul. 19, 2022), <https://www.env.go.jp/content/900453297.pdf>.

³³ ESG Investor, *Japan Proposes Mandatory Climate Risk Disclosure*, regulationasia.com (Sep. 6, 2021), <https://www.regulation-asia.com/japan-proposes-mandatory-climate-risk-disclosures/>.

³⁴ [http://www.treasury.gov.za/comm_media/press/2022/SA Green Finance Taxonomy - 1st Edition.pdf](http://www.treasury.gov.za/comm_media/press/2022/SA%20Green%20Finance%20Taxonomy%20-%201st%20Edition.pdf) (Jul. 18, 2022).

architecture.³⁵ However, nothing has been published on this yet. The 500 largest listed Indian companies are, at least, required to disclose corporate responsibility and sustainability indicators based on the *National Guidelines for Responsible Business Conduct* and as part of Business Responsibility Reporting.³⁶

China, as the biggest country in the world and an east Asian economic power player, puts some focus on ESG compliance. To provide a locally adapted framework for domestic companies, the China Enterprise Reform and Development Society, together with experts from China's leading research institutions and companies, initiated a project to produce a guide to ESG disclosure.³⁷ How effectively this is implemented and by what standards is another matter.

Brazil, which has been criticized for its economic exploitation of rainforests,³⁸ does not seem to have significant ESG activities.

D. Development Outside the Legislative Context

ESG reporting and compliance was originally understood as a voluntary commitment:

“ESG is the acronym for Environmental, Social, and (Corporate) Governance, the three broad categories, or areas, of interest for what is termed ‘socially responsible investors.’ They are investors who consider it important to incorporate their values and concerns (such as environmental concerns) into their selection of investments instead of simply considering the potential profitability and/or risk presented by an investment opportunity. (...) Socially responsible, or ESG, investing may also be referred to as sustainable investing, impact investing, and mission-related investing. ESG investors tend to be more activist investors, participating at shareholder meetings and actively working to influence company policies and practices.”³⁹

Accordingly, the term ESG was popularized in 2004 by the report "Who Cares Wins", a collaborative initiative of financial institutions convened by the UN.⁴⁰ It was supported by 20 well-known institutions. One prominent initiative that grew out of this was the adaptation of the United Nations' 17 Sustainable Development Goals in 2015.⁴¹ Since then, the topic of ESG has gained enormous popularity

³⁵ Bhasker Tripathi, *India's Proposed Sustainable Taxonomy and The Complexity of Weighing Climate Gains with Capital Concerns*, carboncopy.info (Jun. 3, 2022), <https://carboncopy.info/indias-proposed-sustainable-taxonomy-lessons-to-remember-worries-to-address/>.

³⁶ Financial Express, *Navigating the Complexities of ESG Compliance in India*, [financialexpress.com](https://www.financialexpress.com/opinion/navigating-the-complexities-of-esg-compliance-in-india/2275066/) (Jun. 21, 2021), <https://www.financialexpress.com/opinion/navigating-the-complexities-of-esg-compliance-in-india/2275066/>.

³⁷ China Enterprise Reform and Development Society, [cerds.cn](https://www.cerds.cn/site/content/8237.html) (Jul. 19, 2022), <https://www.cerds.cn/site/content/8237.html>.

³⁸ Cristina Müller, *Brazil and the Amazon Rainforest*, Umweltbundesamt GmbH (Environment Agency Austria), (May 2020) S. 24, [https://www.europarl.europa.eu/RegData/etudes/IDAN/2020/648792/IPOL_IDA\(2020\)648792_EN.pdf](https://www.europarl.europa.eu/RegData/etudes/IDAN/2020/648792/IPOL_IDA(2020)648792_EN.pdf).

³⁹ Kyle Peterdy, *ESG (Environmental, Social and Governance)*, Corporate Finance Institute (Jul. 5, 2022), <https://corporatefinanceinstitute.com/resources/knowledge/other/esg-environmental-social-governance/>.

⁴⁰ International Finance Corporation, *Who Cares Wins*, ifc (Aug. 2004), https://www.ifc.org/wps/wcm/connect/9eeb7982-3705-407a-a631-586b31dab000/IFC_Breif_whocares_online.pdf?MOD=AJPERES&CACHEID=ROOTWORKSPACE-9eeb7982-3705-407a-a631-586b31dab000-ikD12B5#:~:text=Who%20Cares%20Wins%28WCW%29%20was%20initiated%20by%20the%20UN,Bank%20Group%20%20were%20among%20the%20endorsing%20institutions.

⁴¹ The United Nations, *The Sustainable Development Agenda*, UN (Jul. 19, 2022), <https://www.un.org/sustainabledevelopment/development-agenda/>.

and developed into a global phenomenon. This is not only shaping the social debate but is also having a significant impact on the investment market. In Germany alone, the total amount of capital investments which took ESG criteria into account rose by 25% in 2020 to a new record volume of 335.3 billion Euro.⁴² This is increasing pressure on companies to operate sustainably. Larry Fink, founder and chairman of BlackRock, addressed the CEOs of German corporations in a letter in January 2020, calling for a stronger focus on ESG issues. Such risks are also investment risks, he said, which is why his company will increasingly include them in investment decisions in the future. This trend is ongoing.⁴³ The two largest EFT providers, BlackRock and Vanguard, offer ESG funds to their clients. BlackRock added six new ESG funds in 2020 and now also employs a Head of Sustainable Investing.⁴⁴

These developments and the activities of national legislators, as set out above, influence each other, as the importance of ESG issues has increased in public discussions and is perceived as urgent, not least because of global climate change. Thus, both legislation and public concern are combining to increase interest in ESG issues.

Courts are also influencing the ESG environment at various levels. A worldwide "climate protection jurisprudence" is developing both at the level of constitutional law and between private parties. This trend was reflected in the Dutch "Shell Decision" and in the injunctive relief currently being sought by the German environmental aid organization Deutsche Umwelthilfe.

Last year, the oil and natural gas company Shell lost a lawsuit in the Dutch District Court in The Hague and was ordered to significantly reduce its carbon dioxide emissions. CO₂ emissions, the court ruled, had to be reduced by 45% by 2030 compared to 2019.⁴⁵ The environmental protection organizations Milieudefensie and Greenpeace were among the plaintiffs. In 2021, Deutsche Umwelthilfe filed lawsuits against three companies demanding that they cease and desist from activities which produce greenhouse gases. In the case of Mercedes-Benz and BMW, Deutsche Umwelthilfe demanded that the sale of cars with climate-damaging internal combustion engines be halted by October 2030, while the Norwegian oil and gas firm Wintershall Dea would be required to cease production of natural gas and crude oil by December 31, 2033.⁴⁶ Large enterprises often produce several times as many greenhouse gases as some nations, and were thus obliged, the lawsuit argues, to adapt their operations to protect the climate and citizens' fundamental rights.⁴⁷ The lawsuits were filed in Germany at the Munich Regional Court, the Stuttgart Regional Court and the Kassel Regional Court. On June 21, 2022, the first hearings occurred before the Stuttgart Regional Court.⁴⁸

⁴² Bayern Invest, *ESG-News*, bayerninvest.de (Jul. 19, 2022), <https://www.bayerninvest.de/maerkte-meinungen/research-news/esg-news/index.html>.

⁴³ Larry Fink, *Letter to the CEOs*, blackrock (Jan. 14, 2020), <https://www.blackrock.com/ch/individual/en/larry-fink-ceo-letter?switchLocale=Y>; Dorothy Neufeld, *New Waves: The ESG Megatrend Meets Green Bonds*, Visual Capitalists, (Aug. 11, 2020), <https://www.visualcapitalist.com/esg-megatrend-green-bonds/>.

⁴⁴ BlackRock, *Welcome to the BlackRock site for institutional investors*, blackrock (Jul. 19, 2022), <https://www.blackrock.com/institutions/en-us/biographies/paul-bodnar>.

⁴⁵ The Hague District Court, C/09/571932 / HA ZA 19-379 (May 26, 2021), <https://uitspraken.rechtspraak.nl/inziendocument?id=ECLI:NL:RBDHA:2021:5339>.

⁴⁶ Deutsche Umwelthilfe, *Wir verklagen Unternehmen für mehr Klimaschutz*, DUH (Jul. 19, 2022) <https://www.duh.de/klimaklagen/unternehmensklagen/>.

⁴⁷ Deutsche Umwelthilfe, *Wir verklagen Unternehmen für mehr Klimaschutz*, DUH (Jul. 19, 2022) <https://www.duh.de/klimaklagen/unternehmensklagen/>.

⁴⁸ Spiegel, *Gericht sieht Klage der Deutschen Umwelthilfe gegen Mercedes kritisch*, (Jun. 21, 2022) <https://www.spiegel.de/auto/deutsche-umwelthilfe-gegen-mercedes-gericht-sieht-klage-kritisch-a-1d01b8d1-12c5-4abf-bddc-f23d11369e26>.

For both cases, it is characteristic that the connecting factor here is not existing damages, but rather future damages. This derives from the argument that “climate protection rights” are aspects of human rights, in particular the right to life (according to Art. 6 of the International Covenant on Civil and Political Rights, ICCPR) and in the right to privacy (according to Art. 17 of the ICCPR).⁴⁹

E. Assessment

Obviously, the topic of ESG has long since been transformed from a voluntary commitment to a “real” compliance issue, backed by laws which impose severe sanctions and court decisions developing a human rights-based approach. Companies must therefore deal with these issues, assess the risks correctly, and draw the right conclusions for the company’s CMS. This is not an easy undertaking, because, as the sections I. A.-D. of this paper have shown, legal obligations are onerous, and enforcement of them by the authorities is strict.

Further, the regulatory schemes are complex. First, we see high level of detail, especially in the area of ESG regulation. National supply chain laws provide an initial insight into the practical problems associated with regulatory ambiguities. This can be exemplified by the German LkSG which served as one model for the EU CSDD Directive. The annex to the German LkSG refers to many international conventions, protocols, and reports on human rights and environmental risks. These add up to 14 sources of “soft law”. Furthermore, the EU CSDD references another 12 UN Guiding Principles, national action plans, OECD guidelines and similar. It is impossible to understand the scope of ESG obligations without addressing these sources.⁵⁰ Second, this high level of detail goes hand-in-hand with much ambiguity. The provisions are brimming with vague terms, including key ideas such as “supply chain”, “company”, “risk analysis”, “risk management”, and “preventive and remedial measures”. Companies which intend to follow the guidelines responsibly quickly come up against these interpretive problems, and legislators and authorities have so far remained largely silent on these essential issues. It can, of course, be argued that interpreting undefined legal terms is nothing new and is even “day-to-day business” in companies and their legal departments. Yet, the challenge is not so much the vagueness of the legal terms *per se*, but the profound intrusion of these terms into the areas of risk analysis and risk management, which traditionally represent a core responsibility – and competence – of companies. We can note, for almost all of the ESG (and also data protection) regulation discussed above, that these laws interfere considerably with corporate decisions on how to conduct risk assessments, how to prioritize and steer risks, including how to organize internal processes, and even how to communicate internally and externally. As noted above, similar burdens attended the implementation of the EU GDPR. The regulation was not so much about substantive increases in data security, but on the development and implementation of internal processes in companies, for example regarding risk assessments, data protection impact assessments, procedures in the event of data breaches, responses to data subject inquiries, and the like. The draft of the EU CSDD Directive goes into a similar direction: Above all, it calls for “human rights and environmental due diligence” which must be integrated into the company’s guidelines and processes. Abuses must be identified and harm prevented. Companies

⁴⁹ Christoph H. Seibt/Marlen Vesper-Gräske, *Lieferkettensorgfaltspflichtengesetz erweitert Compliance Pflichten*, Vol. 10 CB, 357, 358 (2021).

⁵⁰ See also, including for the references, Christoph H. Seibt/Marlen Vesper-Gräske, *Lieferkettensorgfaltspflichtengesetz erweitert Compliance Pflichten*, Vol. 10 CB, 357, 363 (2021).

must establish reporting procedures and review the effectiveness of their measures. The EU CSDD Directive does not plan to sanction any specific behavior such as a human rights or environmental violations. Rather, it specifies (for implementation by national legislators) which risks companies must assess (namely human rights and environmental risks), how they should do so (for example, by developing a code of conduct or through training), and, to a certain extent, provide a sketch of internal processes which would be evaluated as adequate for the purposes of risk management. For instance, the draft Directive prescribes in Art. 10 of the EU CSDD how often risk analyses should occur (“annual review”). This greatly reduces companies' discretion, even though responsible use of this discretion is key to entrepreneurial decision-making, which is ordinarily governed by the principle of legality and, not least, the business judgment rule. The rule defines the scope of entrepreneurial decision-making leeway of managing directors and board members and exempts reasonable decisions made after adequate research from legal challenge. This doctrine, which originated in the U.S., is now also widespread outside the common law and has been applicable law in Germany since around 1997.⁵¹ According to the business judgment rule, managing directors and board members are not liable for the negative consequences of corporate decisions if the decision was made on the basis of adequate information, not driven by extraneous interests, and was made in the good-faith belief that it was in the best interests of the company. This freedom, however, has now been limited by legislators who explicitly removes leeway and requires companies to implement certain approaches to risk management and internal processes. Structurally, we are seeing a legalization of risks, through which the legislator *de facto* eliminates companies' entrepreneurial discretion.

It is further interesting that the focus on risk management and prevention closely resembles developments in "climate protection jurisprudence", which, as noted above, focuses on preventing future harm. In both cases, the spotlight is on prevention, and failures to prevent are sanctioned. Ultimately, therefore, we see a shifting of responsibilities to much earlier points in time.

Another complicating factor is that many of the legislative projects described in section I. A.-D. stand out due to the threat of very high fines. In the run-up to the EU GDPR, for example, the threat of fines coupled with considerable uncertainty about interpretation of legal terms and the horizon of expectations led to a great deal of speculation about how the authorities might react and what fines they might impose. Similar uncertainty surrounds the topic of supply chain due diligence. Even in companies where human rights and environmental protection violations are not obvious or likely, there are considerable worries about what needs to be done to meet the law's requirements. When legal demands are not only vague but also coupled with potentially severe sanctions, as was the case with the EU GDPR in particular, companies often abandon business practices which are actually acceptable or at least subject to oversight, even if these practices are essential for the company's business activity. Such risk avoidance is understandable: Anyone reckoning with fines several times as high as previous sanctions will incur even higher costs trying to avoid them, even if the probability of violation remains the same. Furthermore, risk aversion becomes more likely where the consequences increasingly affect company managers personally.⁵² This forces autonomous entrepreneurial decision-making into the back seat.

⁵¹ See sec. 93 para. 1 sent. 2 German Stock Corporation Act.

⁵² This trend is not only evident in the much publicized „Yates-Memo“ (DOJ, Yates-Memo, justice.gov (Sep. 9, 2015), [https://www.justice.gov/archives/dag/file/769036/download.](https://www.justice.gov/archives/dag/file/769036/download)), but can also be observed in other contexts, see, for example, the German “Siemens/Neubürger” decision“, Regional Court Munich I, Urt. v. 10.12.2013 – 5 HK O 1387/10.

In any case, these laws tie up enormous capacities within companies, since they must deal with the “new risks” in detail. Each new law requires a reassessment of the risks within the company and the required structures, processes, and resources must be determined and analyzed, which requires considerable effort.

In view of the importance of the laws’ aims (such as human rights and protection of the environment), these negative effects could be recognized at least as justifying the demands placed on companies. Good laws should have positive consequences. If these occur, certain “side effects”, such as increased expense or government interference in compliance risk management, can and must perhaps be accepted. But are the aforementioned regulations “good laws” leading to positive consequences, or are they primarily symbolic acts meant to keep companies on their toes? The discussion about the symbolic content of (criminal) law is not new, but it plays out quite variously in different legal systems.

A few examples may help clarify the matter: Even if uniform definitions across national jurisdictions are difficult, “symbolic law” is characterized by the fact that it is directed more towards reassurance than towards effective implementation of specific requirements and changing the behavior of specific addressees:

“Symbolic law means law that its sponsors enact for the sake of enacting the law. It sponsors demanded that law not primarily as an instrument to change behaviors, but to demonstrate to the world (and especially to their constituents) the sponsor’s beliefs.”⁵³

Here, reassurance has primarily a socio-communicative meaning:

“The primary aim of such legislation appears to be reassurance rather than redress, prevention, or punishment. (...) Governments are warming to the notion that it is in part through moral persuasion and debate created by legislation that attitudes and behavior will change.”⁵⁴

In Germany, Niklas Luhmann attributed law to be primarily not a “coercive order, but a facilitation of expectations”.⁵⁵ The criticism of symbolic (criminal) law focuses on legislative legitimacy, when the object of regulation are largely undefined universal legal interests, such as the “economy, environment, taxes, automatic data processing, terrorism, drugs, export of dangerous objects (...) which (...) leave nothing to be desired in terms of generalization”.⁵⁶

In the EU, the awareness of “symbolic law” is found not only on the national but also on EU legislative level: “The discrete presence of symbolic EU criminal law”⁵⁷ reveals that EU institutions are well aware of the expressive purpose of criminal law and conceive legal harmonization as a means to achieve objectives which are not limited to instrumental rationality. The EU may even be a particularly fertile

⁵³ Law Insider, *Symbolic law definition*, lawinsider.com (Jul. 19, 2022), <https://www.lawinsider.com/dictionary/symbolic-law>.

⁵⁴ Catherine Fieschi, *Symbolic laws*, Prospect magazine (Feb. 26, 2006), <https://www.prospectmagazine.co.uk/magazine/symbolic-laws>.

⁵⁵ Niklas Luhmann, *Rechtssoziologie*, 100 (1987).

⁵⁶ Winfried Hassemer, *Symbolisches Strafrecht und Rechtsgüterschutz*, Vol. 12 NSTZ 553, 557 (1989).

⁵⁷ Thomas Elholm and Renaud Colson, *The symbolic purpose of EU criminal law*, p. 7 (Jul. 19, 2022), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2952582.

source of symbolic legislation, which can serve to create political identity:

“The advancement of mutual trust through symbolic legislation is supposed to forge a common culture among professionals but this logic also applies to ordinary people. By imposing on Member States an obligation to criminalize specific types of offenses, the Union seeks to create social consensus by identifying European shared values. (...) by reinforcing common moral norms, the European Union take a step towards a thicker social and political notion of European citizenship (...) to build ‘the supranational demos’ which Europe is repeatedly said to lack.”⁵⁸

It is thus probably no coincidence that the focus of current EU compliance legislation is ESG. The EU's attempts to pass laws in this strongly values-driven domain (human rights, environmental protection, diversity, etc.) are unquestionably important, but not very contoured because the underlying values are so general by nature.

Another strategy of legislators, especially in the EU, is also emerging in the legislative domains discussed above, namely the strategy of indirect behavioral control. Companies are to be encouraged to be more “sustainable”. Sustainable behavior is meant to be incentivized through regulation, which reflects the above discussion of the shift from reaction to prevention. Whether incentivization works is, however, questionable. Further, the assessment of what is good (sustainable) and bad (not sustainable) can quickly falter due to political and economic circumstances. The Russian war against Ukraine, for instance, has led to a boom in the arms industry. Likewise, the assessment of nuclear energy as sustainable under EU Taxonomy conflicts with the previous view: France pushed to have nuclear power, which is CO₂-free and a key energy source in France, classified as a sustainable activity which addresses climate change.⁵⁹ In early July 2022, the EU Parliament approved this classification regarding gas and nuclear power. Austria already announced that it would file a lawsuit against the decision.⁶⁰

However, symbolic legislation and incentives (if they work) may well be useful side effects of an understanding of the law which moves away from (reactive) sanctions more in the direction of (preventive) behavior changing.⁶¹ But this is not experimental ground: We have already seen that the threat of severe sanctions clearly underlines the seriousness of the legislative ambitions and, at least in the area of the EU GDPR, that the law is also enforced. We are therefore dealing with complex, predominantly fuzzy, value-driven, symbolically-charged and preventive laws that are anything but “dead letters”. They intervene deeply in corporate risk management, aim to change behavior, and definitely have sharp “teeth”. It is therefore legitimate to ask how such laws will function and if they deliver what they promise. If they fail to achieve their declared and worthy goal of strengthening human rights, protecting the environment, and strengthening data protection and security, their heavy impact on

⁵⁸ Thomas Elholm and Renaud Colson, *The symbolic purpose of EU criminal law*, p. 8 et seq., with further references (Jul. 19, 2022), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2952582.

⁵⁹ Rick Noack, *Is nuclear energy green? France and Germany lead opposing camps*, washingtonpost.com (Dec. 18, 2021) <https://www.washingtonpost.com/world/2021/12/18/nuclear-energy-climate-france-germany/>.

⁶⁰ Zeit Online, „Österreich will Klage gegen Ökolabel für Atom- und Gaskraft einreichen“, (Jul. 6, 2022), https://www.zeit.de/wirtschaft/2022-07/taxonomieverordnung-oesterreich-klage-oeko-label-eu-parlament-eugh?utm_referrer=https%3A%2F%2Fwww.google.com.

⁶¹ Catherine Fieschi, *Symbolic laws*, prospectmagazine (Feb. 26, 2006), <https://www.prospectmagazine.co.uk/magazine/symbolic-laws>.

companies – particularly in the current crisis situations of the pandemic, the war in Ukraine and rising energy prizes – they will not be easy to justify.

Reliable answers to the effect of ESG legislation will only be possible once the national laws have been implemented and concrete experience with official prosecution and sanctioning as well as judicial review has been gained.

II. COMPANIES' STRATEGIES FOR IMPLEMENTATION

Until such clarity is available, companies will have to adapt to the developments described, such as the density of regulation, interventions in risk management and the design of compliance processes. In doing so, they are pursuing very different strategies.

Some companies, particular smaller ones, are often overwhelmed by the volume and complexity of the regulations in areas such as ESG and data protection. They intuitively perceive these laws as exaggerating risks, setting hurdles at random, or being generally “not realistic”. These companies are more inclined not to comply, mainly because they see no harm in disobeying the laws. They do not believe they are exposed to these risks and doubt that conducting complex risk assessments will benefit the company, shareholders, employees, or, for that matter, genuinely achieve goals in the areas of human rights or the environment. Other companies intend to comply but are still unclear about the details. They see laws which intervene deeply into company risk management without specifying exactly what companies are supposed to do. Often these corporations end up taking only half-hearted measures, or only performing minimal compliance to avert negative publicity.

Some companies, mainly larger ones, invest in ESG compliance, often as a reaction to grievances and scandals. Volkswagen recently appointed a new human rights officer in light of the allegations regarding its production in China. The specific concern is the VW plant at the Urumqi location in the western province of Xinjiang, which is operated together with the Chinese state-owned company SAIC. China has been criticized for years for its treatment of its Muslim Uyghur minority. According to human rights activists, hundreds of thousands of people have been sent to so-called re-education camps in Xinjiang.⁶²

Finally, some companies, follow a certain trend, symbolically charge compliance measures with ESG content. Priority is often given to issues that enhance the company's image and meet the expectations of shareholders and stakeholders, as well as employees. One example is the ESG campaign of ice cream manufacturer Ben & Jerry's, which labels several general ESG topics as “Issues We Care About” and promotes initiatives in areas such as refugee treatment, fair trade, climate justice, peace-building, marriage equality, and vegetarianism.⁶³

⁶² BBC, *Who Are the Uyghurs and Why is China Being Accused of Genocide?*, BBC.com (May 24, 2022), <https://www.bbc.com/news/world-asia-china-22278037>. Following the coverage, the *Uyghur Forced Labor Prevention Act* (see I. B.) was released.

⁶³ Ben & Jerry's, *Issues We Care About*, benjerry (Jul. 19, 2022), <https://www.benjerry.ie/values/issues-we-care-about>.

III. RECOMMENDATIONS FOR COMPANIES

Part II shows the various ways companies can deal with increasing compliance requirements. The Ben & Jerry's example also shows that compliance and marketing can be blurred, and a line between the two is not always easy to draw. This also highlights that the compliance area has always been susceptible to a certain symbolism, and not only since the ESG trend emerged. It is well known that compliance goes beyond the mere letter of the law.⁶⁴ Compliance standards often talk about "compliance culture",⁶⁵ which is reflected in the oft-cited nostrum in compliance trainings which holds that "we don't have to do everything we're allowed to do". This approach is generally the right one. A CMS must find its foundation in the lived values of a company. After all, employees must be empowered to make complex decisions for the company about "right and wrong" and do so independently and on their own responsibility. In order to achieve that, they must understand what the declared interests of the company are and which underlying values and objectives play a role. As far as they follow the law, companies are also free to decide which values and which measure are right for them and the resulting corporate identity can certainly contribute to the brand. However, within an environment of burgeoning regulatory expectations which keeps companies in a continuous "pressure cooker" situation, it would be wise to approach the issue with realistic expectations.

Even if legislators are increasingly intervening in the way companies carry out risk analyses and altering the priorities they set, companies should defend their discretion and use it wisely. It is commonplace that risk of loss and profit opportunities are closely linked. Ignoring hazards – especially those that threaten a company's existence – can have fatal consequences. The same applies to overemphasizing them. It is therefore important to carefully examine the real risks and use discretion responsibly. A diligent risk analysis, carefully aligned to a company's situation and needs, is always a good starting point. It typically requires an investment, but it also can free up resources to be invested in measures which don't address real risks. It can identify activities companies should refrain from or indicate areas of lower tangible risk exposure. Knowing the law and the company's operations perfectly, is a prerequisite for a professional risk assessment. Even if laws intrude, there is still a space for responsible and balanced decision-making with regard to risk assessment and prioritization. It might be that ESG topics are very pertinent for a company, but maybe other issues are more pressing. Corruption, for instance, remains one of the greatest threats to global markets. On January 25, 2022, Transparency International released its Corruption Perception Index (CPI) for 2021, covering 180 countries ranked on a scale from 0 (high level of perceived corruption) to 100 (no perceived corruption).⁶⁶ Last year, the global score remained unchanged for the tenth consecutive year at 43 out of 100. Two-thirds of the 180 countries and territories in the study have a serious corruption problem and do not even reach the halfway point of the index.⁶⁷ This is a good reason for companies to continue to take anti-corruption compliance very seriously and not automatically place it behind ESG or data protection.⁶⁸ In any case,

⁶⁴ Wolfgang Leyk, *Compliance als wirtschaftliche Praxis*, in *Corporate Compliance, Handbuch der Haftungsvermeidung im Unternehmen* § 12 Rn. 1. (Hauschka/Moosmayer/Lösler, 3rd edition, 2016).

⁶⁵ For instance, ISO 37301, sec. 5.1.2.

⁶⁶ Transparency International e. V., *Corruption Perception Index 2021*, Transparency International (Jan. 25, 2022), <https://transparency.am/en/cpi/2021>.

⁶⁷ Transparency International e. V., *Corruption Perception Index 2021*, Transparency International (Jan. 25, 2022), <https://transparency.am/en/cpi/2021>.

⁶⁸ Transparency International e. V., *Corruption Perception Index 2021*, Transparency International (Jan. 25, 2022), <https://transparency.am/en/cpi/2021>. However, analyses also show that there is a close link between fighting corruption and respecting human rights. In most cases, more corruption can lead to restrictions on civil liberties, while fewer civil liberties make it more difficult to fight corruption.

companies are well-advised to look at their tangible risks and not to follow trends which push compliance – sometimes – over the line into marketing. They are free to do that of course but should remain aware of why they are doing it.

Finally, depending on the type of business activity and its specific framework, there will always remain risks that the best risk management cannot eliminate. The goal should be “decision-oriented risk management” which incorporates the results of the risk analysis into the decision-making process in accordance with the business judgment rule.⁶⁹ If this step is carried out carefully after an honest and unbiased examination of genuine risks, an effective CMS can be developed for the companies to comply with the law and implemented with entrepreneurial responsibility.

⁶⁹ Werner Gleißner, *Business Judgement Rule*, GRC 2019, 148 (2014).