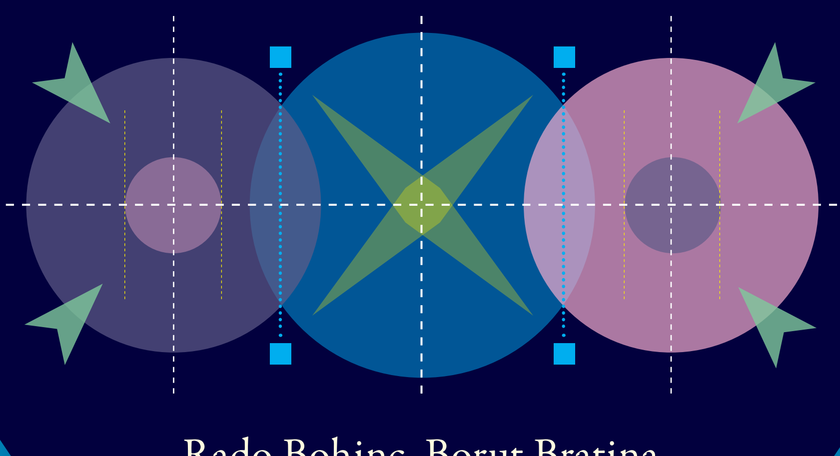
Recent Challenges in Corporate Governance



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Content

Editorial Preface

This monograph is a collection of contemporary critical views on corporate governance in the 21st century in terms of both social responsibility and sustainable development, as well as efficiency and adaptation to modern business flows. A series of anachronisms is identified, which has emerged due to clinging on to classical property rights approaches and neglecting civilisational challenges, whose shared feature is that the value relations between the increasingly dominating highly intellectual work and capital in modern society are changing rapidly.

First presented in the monograph are the genesis, values, controversies and challenges of corporate governance in the EU, with the analysis revealing several shareholder controversies (Bohinc). The position of shareholders in different types of companies varies considerably, where especially the position of those in the financial sector is substantially dissimilar. The level of shareholders' rights depends on the kind of shares they hold; shareholders' rights are however not based on property but on the company–shareholder contractual relationship and the kind of shares (financial instruments) they have bought. Shareholder democracy is in fact the crucial reason for the inequality of persons holding shares in terms of their power to affect the company's governance. Property rights are attached to shares rather than to the individuals holding them (property democracy rather than people's democracy).

The monograph next considers the question of **whether we really need stronger shareholders' engagement only** (Bohinc), arguing that shareholder activism is a central issue in modern corporate governance. Ownership concentration leads to shareholder activism that causes short-termism in the maximisation of profits as one of the major explanations for a company's inefficient and poor business performance in the long run. Disregarding the structural measures so as to strengthen the position of the employees whose long-term stability is of the greatest natural interest is a huge shortcoming of all anti-short-terminist measures in the conduct of management and shareholders; this has its roots in the ideological systemic exclusion of employees from decision-making. According to the EU, the key corporate governance deficiencies related to the behaviour of companies, their boards and shareholders (institutional investors, asset managers, intermediaries, proxy advisors) are the insufficient engagement of institutional investors and asset managers and the inadequate transparency of proxy advisors. No measure has tackled the position of the employees in corporate governance. The measures are primarily related to overcoming short-sightedness and improving the quality of shareholder decision-making, notably in the relationship between the intermediaries of institutional owners and asset managers. Measures to involve those most interested in the long-term success of the corporation, because their existence depends on it, i.e., the employees, are not taken in either the EU's measures or those of the OECD. The ideological barriers are too great.

The monograph then moves on (Bratina, Podgorelec) to systematically show the **duties of the management and supervisory board members** and examines the current development of their liability on both legislative and case-law levels. On the legislative level, a problem exists in the form of the 10-year limitation period. Another problem addressed in this part of the monograph is the legal protection of shareholders/company members of subsidiaries when the majority holdings are not held by a company but by a different legal subject, e.g., by a state or a municipality. In this respect, suitable solutions are proposed. The authors criticise the existing case law as concerns rulings on the said criminal offence in connection with one-person limited liability companies.

As Tičar and Primec note in the monograph, **the effectiveness of corporate governance is no longer judged solely according to short-term financial returns**. Shareholders and the broader social community are increasingly demanding long-run value creation and non-financial performance. Corporate social responsibility has become a global phenomenon addressed by academics and major international organisations, including the OECD and the EU. Directive 2014/95/EU introduced the obligation for large public interest corporations to report certain non-financial information, making it the first legal act on corporate social responsibility. In this part of the monograph, the authors review the current practice regarding non-financial reporting in the EU and present the main highlights of the new CSD.

According to Svetina and Ruparčič, **corporate social responsibility (CSR) is a coherent force of modern entrepreneurship** and the proper answer to today's challenges. CSR helps reassure society by advocating both free economic initiative and social responsibility with regard to environmental, social and universal social issues. Above all, the social responsibility of entrepreneurs and business people is in their own interest since it raises awareness of the importance of their work and the contribution they make to the community. Their image is thereby strengthened. Companies that accept CSR are thus more successful. These are positive synergies within society. The authors see CSR as a way of governance (societal and corporate) that considers the social consequences of a governance decision as being just as important as the economic ones (profit-making).

As described by Črepinko, Bratina and Festić, **banks and financial organisations are playing a vital role in the ongoing recovery from the crisis**, including by influencing the development of corporate governance. The legal provisions are binding on all market participants and sanctions may be expected in the event of a breach which, in turn, gives investors some legal certainty. Centralised systems are typically coordination systems, while decentralised systems are usually protective systems. Which system prevails depends on the existence and character of the institution, as well as on the courts, lawyers, law enforcement agencies, trade unions and business groups. It is important to note that the biggest differences in the practice of implementing corporate governance do not stem from the recommendations of the Corporate Governance Codes, but from the different corporate and securities law regimes.

According to Jovanovič, reporting or, more broadly, the **disclosure of remuneration policy** has been added to the very concept and scope of remuneration policy. This forms part of the general policy of the company and hence disclosure is important for both internal and external stakeholders. Since corporate law, and corporate governance in particular, regulates the relationship between the management body (management or supervisory board), the supervisory body (supervisory board or board of directors), shareholders and stakeholders of the company (other stakeholders), corporate institutions must operate in tense relations of the rights and obligations of company bodies in order to improve the corporate environment and thus corporate governance itself. Namely, as the author states, corporate governance also determines the structure (organisation) that supports the company's goals, the means to achieve them, and monitoring of the results. The purpose of corporate governance is to help create an environment of trust, transparency and accountability which promotes long-term investment, financial stability and business integrity, thereby also supporting stronger growth and the development of a more inclusive community.

Researchers, practitioners and the general public will find the monograph to be an interesting read, especially those who have followed corporate governance developments in recent decades and are looking for development solutions better suited to the rapidly changing business approaches enabled by the digitisation of business life and required in the green transition. We hope the innovative suggestions made in the monograph encourage policymakers to introduce measures to overcome the shortcomings and controversies in corporate governance.

Editor

GENESIS, VALUES, CONTROVERSIES AND CHALLENGES OF CORPORATE GOVERNANCE IN THE EU

Rado Bohinc

Summary

The harmonisation of EU company law has not always been successful. Convergence or divergence is a permanent dilemma with EU company law. The constant and numerous amendments to corporate legislation made by member states are largely due to following and implementing the EU's corporate regulations. This means that there are no original and innovative solutions based on national peculiarities and traditions.

The article first outlines a number of **shareholder controversies**. The position of shareholders in different types of companies varies considerably, notably that of shareholders in the financial sector. The level of shareholder rights depends on the kind of shares they hold; shareholders rights are however not based on property but on the company–shareholder contractual relationship and the kind of shares (financial instruments) they have bought. The most fundamental decisions of the company are left to all shareholders, including those who have just acquired their shares and have no idea at all of the company's performance. Yet, employees do not enjoy ex-ante rights like minority shareholders do (e.g., placing items on the agenda of the shareholders' meeting), nor ex-post rights (to seek redress in shareholders' court actions once rights have been violated).

The article then discusses **ownership structures and shareholder democracy**, establishing that shareholder democracy is in fact the key reason for the inequality of persons holding shares in terms of their power in the company's governance. Property rights are attached to shares rather than to the individuals holding them (property democracy rather than people's democracy). Ownership concentration leads to shareholder activism that causes short-termism in the maximisation of profits as one of the biggest reasons for explanations for a company's inefficient and poor business performance in the long run. Although the company law concept (legislative framework for directors' duties and liabilities) does not provide a basis for shareholder activism, it also does not successfully prevent it. The activism of shareholders and managerial short-sightedness (myopia) in the decision-making process in concentrated ownership companies is not even expressly legally prohibited. The votes of shareholders who are not part of the controlling (voting) bloc (51% or even 75%) do not count at all despite formally enjoying all

property rights and participating in all decision-making procedures. A mainly institutional ownership structure in terms of size and, especially, political influence on decision-making is very typical in the economies of post-privatisation countries. In countries previously in transition, internal (employee) ownership does not work well and has been decreasing since privatisation. Shareholder democracy is not intended for small shareholders like employees. With shareholder democracy, only the big who enjoy majority rule manage to take power, prosper and win. This is leading to the disappearance of the shareholdings of employees as small shareholders.

Key words: EU company law, corporate governance, ownership structures, shareholder democracy short-termism, intermediaries, institutional owner asset managers, employees.

1. Introduction

1.1 The OECD's definition of corporate governance

Corporate governance around the world is far from unified. Similarly, corporate law is only partly harmonised in the EU, although there is growing convergence in certain areas. However, much has been achieved in the area of non-binding recommendations for the governments and corporations of the most developed countries.

One may find several **definition**s of corporate governance whose underlying approaches are different. Corporate governance is most often defined in a narrower sense (structure, powers and responsibilities of bodies) and a broader sense (the whole relationship between society, stakeholders and bodies). The OECD Principles of Corporate Governance[1] provide specific guidance for legislative and

1 OECD (2015), G20/OECD Principles of Corporate Governance, OECD Publishing, Paris. The OECD Principles 2015 contain the results of the second review of the Principles 2004, conducted in 2014/2015. The Principles' focus is on publicly traded companies (financial and non-financial). However, they might also be a useful tool for improving corporate governance for privately held and state-owned enterprises.
http://dx.doi.org/10.1787/9789264236882-en

regulatory initiatives in both OECD and non-OECD countries. The following **values** provide the basis for a well-functioning corporate governance system: a high level of transparency, accountability, board oversight, respect for the rights of shareholders, and respect for the role of key stakeholders.

According to the OECD's Principles, **corporate governance** involves a **set of relationships** between a company's management, its board, shareholders and other stakeholders. Corporate governance provides the structure through which the objectives of the company are set (the board pursues objectives that are in the interests of the company and its shareholders) and the means for accomplishing those objectives and monitoring performance. **The OECD's**[2] **Principles follow a broader definition that covers six different fields:** I) Effective corporate governance framework; II) The rights and equitable treatment of shareholders and key ownership functions; III) Institutional investors, stock markets, and other intermediaries; IV) The role of stakeholders; V) Disclosure and transparency; and VI) The responsibilities of the board.

1.2 Fields and tools for a harmonised company law approach across the EU

There are 27 different national company laws in the EU. All of this legislation **addresses domestic companies as well as foreign entities** operating in Member States. Implementation of the right of establishment for companies which, under Article 54.1 of the TFEU, are to »be treated in the same way as natural persons, who are nationals of Member States« is difficult to solve with **comply with and explain** recommendations only. There are views[3] that a

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The OECD Principles 2015 contain the results of the second review of the Principles 2004 conducted in 2014/2015.

2 See: OECD Principles of Corporate Governance (2015), OECD Guidelines for Multinational Enterprises (2011) and OECD Guidelines for state owned enterprises (2004). See also: OECD Declaration on International Investment and Multinational Enterprises of 27 June 2000; 27 June 2000.

3 The 2011 Action Plan for European company law (COM (2011) 164: GREEN PAPER, The EU corporate governance framework, final) urges for more decisive action on the EU level.

greater number of elements of company law should be dealt with on the European level in a **binding form** to ensure a more harmonious approach across the EU.

Well-functioning corporate governance is in the interest not only of countries where companies are based but also of the countries in which they operate. This means that **equivalent protection** for both **shareholders and creditors** of public limited liability companies **is crucial**. In addition, the coordination of national provisions relating to disclosure and reporting requirements, the formation of companies, and to the maintenance, increase or reduction of their capital is particularly important[4].

Following implementation of the **right of establishment,** with a view to ensuring **safeguards** for the protection of the interests of companies and others, **equivalent coordination throughout the EU** is provided for in Article 50(2)(g) of the TFEU. Companies or firms constituted under civil or commercial law, including cooperative societies, and other legal persons governed by public or private law, except those which are non-profit-making) shall accordingly be **treated in the same way as natural persons** who are nationals of Member States.

Harmonisation of the rules relating to company law is essential for the functioning of the EU's internal market. The objectives of efforts to this end stated in EU documents include: providing equivalent protection for shareholders and other parties concerned with companies, ensuring freedom of establishment for companies across the EU, fostering the efficiency and competitiveness of businesses, and promoting cross-border cooperation between companies in different Member States.

EU company law mostly comprises the following **legal tools:** directives, regulations and recommendations. **These legal tools cover a range of company law matters such as:** disclosure and transparency, formation and maintenance of capital, increases or decreases of the capital, own shares, mergers, divisions (also cross-border), takeovers, the exercise of shareholder rights, annual accounts,

4 Public limited liability companies predominate in the economy of EU Member States; public limited liability companies' activities frequently extend beyond their national boundaries. Non-national shareholders hold around 44% of the shares in EU listed companies (most are institutional investors and asset managers). A significant number of listed companies engage in activities in several EU Member States.

consolidated accounts, statutory audits, auditors' independence and international accounting standards, branches etc. It also covers certain **specific EU forms of companies** and other entities like the European Company (Societies European), the European Cooperative Society and the European Economic Interest Grouping.

The harmonisation of EU company law has not always been successful. **Convergence or divergence is a permanent dilemma** with trends and developments in EU company law; and here one might ask: Is **harmonisation opposed to competition**? Although the EU's earlier attempts at the full harmonisation of company law failed, this does not mean that Europe can do without harmonisation. A considerable amount of convergence towards the shareholder-oriented model of the corporation has occurred and is the reality in the EU. However, the forces of market competition and institutional shareholder activism have thus far been stronger than those of harmonisation.

Moreover, the harmonisation of employee participation in governance and profit-sharing in EU law has almost completely failed, and with some exceptions (e.g., European public limited company, European Works Council) is not part of corporate governance. Yet, in the field of financial participation one can find many recommendations, communications and reports, i.e., non-binding documents.

1.3 The EU harmonisation process (1968–2001)

Harmonisation of the EU Member States' company laws is a process that has been **substantially shaping national company laws** over the last **50 years.** It started in the **late 1960s** (1968) with the so-called **First (disclosure) directive** (1968), followed by a further nine directives, totalling **10 in the first 20 years, namely:**[5] The **First** directive**,** in addition to **disclosure** issues for limited companies, dealt with the issues of the **validity of contracts** and **nullity** of companies; the **Second** Council Directive on Capital requirements dealt with the maintenance and alteration of the **capital** of public

5 First Council Directive 68/151/EEC of 9 March 1968 amended by Directive 2009/101/EC of 16 September 2009, for disclosure requirements for branches, see: Eleventh Council Directive 89/666/EEC of 21 December 1989.

limited companies (1977)[6]; the **Third** Council Directive from the late 1970s and **Sixth** Council Directive from the early 1980s provided rules on **mergers** (1978) **and divisions** (1982) of public limited companies;[7] the **Fourth** Council Directive on **annual accounts** of certain types of companies (1978)[8] was also enacted in the late 1970s, followed by two additional accounting directives in the mid-1980s (1983, 1984) on consolidated accounts of companies with limited liability and on the approval of persons responsible for performing statutory audits of accounting documents[9]. **Two more EU legal acts** were approved in the late 1980s: the Regulation on **European economic interest grouping**[10] (1985) and the Directive on disclosure requirements with respect to **branches** (1989).[11]

The harmonisation process in the first period was a success; it contributed to national company laws developing in the same directions for all EU Member States at the time. It also influenced the company law in countries in the process of preparing to join the EU. The **Twelfth** Council Company Law Directive on single member private limited liability companies (1989) was also enacted in this period.[12]

Over the next few years, the **harmonisation process slowed down somewhat**. Until the start of the new millennium, we can only mention Council **Directive on the establishment of a European Works Council from 1994**[13.] In the early period of the new

6 Second Council Directive 77/91/EEC of December 1976 as last amended by Directive 2006/68/EEC.

7 Third Council Directive 78/855/EEC of 9 October 1978, Sixth Council Directive 82/891/EEC of 17 December 1982.

8 Fourth Council Directive 78/660/EEC of 25 July 1978, Seventh Council Directive 83/349/EEC of 13 June 1983, Eighth Council Directive 84/253/EEC of 10 April 1984 and later amendments.

9 Seventh Council Directive 83/349/EEC of 13 June 1983, Eighth Council Directive 84/253/EEC of 10 April 1984.

10 Regulation (EEC) No 2137/85 – the European Economic Interest Grouping.

11 Eleventh Council Directive 89/666/EEC of 21 December 1989 concerning disclosure requirements with respect to branches.

12 Twelfth Council Company Law Directive 89/667/EEC of 21 December 1989, Directive 2009/102/EC of 16 September 2009.

13 COUNCIL DIRECTIVE 94/45/EC of 22 September 1994 on the establishment of a European Works Council or a procedure in Community-scale

millennium, the **Regulation on the statute for a European Company** and the Directive on **corporate governance in a European company** were introduced (2001)[14] along with the **Regulation** on the **Statute for a European company** (2001) (SE).[15]

1.4 The simplification and modernisation process (2002–2020)

The 2002 Action Plan: Simplifying and improving the regulatory environment[16] set out several actions aimed at creating a **new legislative culture** based on the »**better regulation« principle**.[17] In the field of company law, **two directives were simplified: the second company law Directive** on the formation of public limited liability companies and the maintenance and alteration of their capital[18], and **the third and sixth company law Directive** on mergers

undertakings and Community-scale groups of undertakings for the purposes of informing and consulting employees; see also: **Council Directive 97/74/EC of 15 December 1997 extending to the United Kingdom of Great Britain and Northern Ireland, Directive 94/45/EC on the establishment of a European Works Council or a procedure in Community-scale undertakings and Community-scale groups of undertakings for the purposes of informing and consulting employees.**

14 Council Regulation (EC) No 2157/2001 of 8 October 2001 on the Statute for a European company (SE) and Council Directive 2001/86/EC of 8 October 2001 supplementing the Statute for a European company with regard to the involvement of employees.

15 **Council Regulation (EC) No 2157/2001 of 8 October 2001 on the Statute for a European company (SE).**

16 Communication of 5 June 2002, Action Plan »Simplifying and improving the regulatory environment« [COM(2002) 278 final, European Commission (EC). See also: Communication from the Commission of 6 June 2002 - »European Governance: better law making [COM(2002) 0275 final; this Communication complements the Action Plan »Simplifying and improving the regulatory environment«.

17 See also: Communication on Smart regulation in the EU, COM (2010) 543 final, 8 October 2010 and Communication on Regulatory Fitness and Performance (REFIT): Results and Next Steps COM (2013) 685 final of 2 October 2013.

18 Directive 2006/68/EC of the European Parliament and of the Council of 6 September 2006.

and divisions[19]. Directive 2017/1132 of 14 June 2017 **relating to certain aspects of company law** (the **codification directive)** also followed this direction.

The **2003 Action Plan** on **Modernising Company Law and Enhancing Corporate Governance** in the EU (hereinafter the 2003 Action Plan)[20] launched several initiatives as well. **EP Resolution of 21 April 2004 expressed support for the strengthening of shareholders' rights**, particularly through the rules on transparency, proxy voting rights, the possibility of participating at general meetings via electronic means, and ensuring that cross-border voting rights can be exercised.

A considerable number of rules concerning **corporate governance and shareholders' rights** were introduced in the ensuing period, notably: Directive of 21 April 2004 on **takeover bids**[21]; Directive of 26 October 2005 **on cross-border mergers** of limited liability companies;[22] and Directive of 11 July 2007 on the exercise of **certain rights of shareholders** in listed companies.[23]

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amending Council Directive 77/91/EEC as regards the formation of public limited liability companies and the maintenance and alteration of their capital.

19 **Directive 2007/63/EC of the European Parliament and of the Council of 13 November 2007 amending Council Directives 78/855/EEC and 82/891/EEC as regards the requirement of an independent expert's report on the occasion of the merger or division of public limited liability companies** and DIRECTIVE 2009/109/EC of 16 September 2009 amending Council Directives 77/91/EEC, 78/855/EEC and 82/891/EEC, and Directive 2005/56/EC as regards reporting and documentation requirements in the case of mergers and divisions amending Directives 78/855/EEC and 82/891/EEC.

20 Action Plan of the European Union [Communication from the Commission to the Council and the European Parliament Modernising Company Law and Enhancing Corporate Governance in the European Union - A Plan to Move Forward, COM (2003) 284 final] and the subsequent consultation on future priorities for this Action Plan carried out in 2005 and 2006 (hereinafter the Action plan 2012).

21 Directive 2004/25/EC of the European Parliament and of the Council of 21 April 2004 on takeover bids.

22 Directive 2005/56/EC of the European Parliament and of the Council of 26 October 2005 on cross-border mergers of limited liability companies (Text with EEA relevance).

23 Directive 2007/36/EC of 11 July 2007 on the exercise of certain rights of shareholders in listed companies.

Two recommendations can also be considered as a follow-up of the 2002 Action Plan:[24] Commission **Recommendation** of 15 February 2005 on **the role of non-executive or supervisory directors**[25] and Commission Recommendation of 30 April 2009 complementing Recommendations 2004/913/EC and 2005/162/EC regarding the **remuneration of directors.**

1.5 Company law developments in Slovenia

The Law on Commercial Companies of 1993 (hereinafter the LCC) is the most comprehensive and one of the most important laws to be enacted since the country's independence in 1991. In August 2006, the LCC was replaced by the new Law on Commercial Companies of 2006 (ZGD-1), the LCC-1. Since then, almost annually and in line with EU legislation the LCC-1 was amended or corrected by the following laws and Constitutional Court decisions[26].

24 Commission Recommendation 2009/385/EC of 30 April 2009 complementing Recommendations 2004/913/EC and 2005/162/EC as regards the regime for the remuneration of directors of listed companies (OJ L 120, 15.5.2009, pp. 28–31).

25 Commission Recommendation 2004/913/EC of 14 December 2004 fostering an appropriate regime for the remuneration of directors of listed companies (OJ L 385, 29.12.2004, pp. 55–59).

26 Correction of the Companies Act – ZGD-1 (Official Gazette of RS, No. 60/06 of 9 June 2006), Act Amending the Companies Act – ZGD-1A (Official Gazette of RS, No. 10/08 of 30 January 2008), LCC-1A. Act Amending the Companies Act – ZGD-1B (Official Gazette of RS, No. 68/08 of 8 July 2008), LCC-1B. Act Amending the Companies Act – ZGD-1C (Official Gazette of RS, No. 42/09 of 5 June 2009), LCC-1C. Companies Act – official consolidated text – CA-1-UPB3 (Official Gazette of RS, No. 65/09 of 14 August 2009), OCT-UPB3. Law on Amendments to the Companies Act – ZGD-1D (Official Gazette of RS, No. 33/11 of 3 May 2011), LCC-1D. Law on Amendments to the Companies Act – ZGD-1E (Official Gazette of RS, No. 91/11 of 14 November 2011), LCC-1E. Act Amending the Companies Act – ZGD-1F (Official Gazette of RS, No. 32/12 of 4 May 2012) LCC-1F. Act Amending the Companies Act – ZGD-1G (Official Gazette of RS, No. 57/12 of 27 July 2012) LCC-1G. The annulment of the first to fourth paragraphs of Article 10a and the fourth paragraph of Article 10b, and partly repealing the seventh paragraph of Article 10a of the LCC, and the finding that the fifth and sixth paragraphs of Article 10a, part of the seventh paragraph of Article 10a and the first to third paragraphs of Article 10b

The constant amendments to the corporate legislation in Slovenia are not a sign of a tendency to progress and adapt to changing circumstances due to technological development, but are generally to pursue and implement the EU's corporate regulations. This means that there are no original and novel solutions based on national peculiarities and traditions.

Slovenia's Law on Commercial Companies builds on the European tradition in this field. More specifically, it follows the German Aktiengesetz and hence many institutions including management at its own responsibility; the two-tier governance system, and employee participation in management and supervisory boards are similar and comparable to those of Germany and Austria.

There is clearly a long and rich tradition of employee participation in Slovenia. In fact, the previous self-management system that ultimately proved to be economically inefficient, and thereby politically unsustainable, was based on a contractual economy as opposed to a market economy, and labour rights as opposed to the concept of property rights[27]. That tradition, together with the German (Austrian) tradition which for historical reasons prevails as a legislative pattern in the corporate law, caused the Slovenian legislators to follow and even exceed not merely the German two-tier system, but also its employee participation model.

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and twelfth indent of Article 50 of the companies Act insofar as it relates to the first and second paragraphs of Article 10b of the Companies Act are not inconsistent with the Constitution (Official Gazette of RS, No. 44/13 of 24 May 2013). Act Amending the Companies Act – ZGD-1 H (Official Gazette of RS, No. 82/13 of 8 October 2013), LCC-1H. Act Amending the Companies Act – ZGD-1I (Official Gazette of RS, No. 55/15 of 24 July 2015), LCC-1I. Act Amending the Companies Act – ZGD-1J (Official Gazette RS, No. 15/17 of 31 March 2017). Act Amending the Companies Act – ZGD-1K (Official Gazette of the Republic of Slovenia, No. 18/21 of 9 February 2021).

27 The Law on Commercial Companies of 1993 replaced the Enterprise Law enacted in the last period of former Yugoslavia (1988) that attempted to introduce, for the first time after five decades of social and state ownership, as well as traditional property-rights-based legal forms of companies. Legal forms of the former system, based on the Law on Associated Labour (1976) and contract rather than a market economy (associations of labour and later social enterprises), were labour managed or self-managed and not at all comparable with the traditional US corporation.

Under the LCC-1993, a Supervisory Board was made compulsory for companies meeting certain conditions imposed by law related to the size of a company, the number of its employees and shareholders, the way it was founded, and whether it was listed on the Stock Exchange. In smaller Slovenian public companies and in private companies, it was left to the founders to decide whether or not to prescribe a Supervisory Board in the Articles of Incorporation. In 2006, the system of compulsory two-tier corporate governance was abandoned. Nevertheless, the two-tier system continues to prevail in Slovenia today.

The LCC-1 prescribes the basic rules for the founding and operating of companies, sole proprietors, related persons, subsidiaries of foreign companies and the restructuring of their status. The LCC defines the concept and types of commercial companies (including partnerships), the legal personality of a company, its activities, liability, registered name, representation, business secrets and issues regarding the entry of a company on the court register. The most extensive regulations refer to PLC, which include issues such as: the capital and shares, management and governing bodies of a PLC (management board, supervisory board, board of directors), shareholders' meetings, including minority rights, and different kinds of auditing (such as special and extraordinary audits).

To mention only more **recent developments**, following Directive (EU) 2017/828, the **identification of shareholders** is set out in new Articles 235.a to 235.g of the LCC-1 K (2021), taking special account of the fact that different financial intermediaries may be involved as holders; they may even be involved in several stages of a »chain of intermediaries« with the aim of enabling these companies' shareholders to more effectively exercise their corporate rights by providing them with the necessary advance information.

Information and facilitation of the exercise of **shareholders' rights** is regulated in new Articles 235a et seq.); a clear distinction between the actual shareholder and the one who keeps the share for him/her (keeps it on their behalf or otherwise manages it). A new definition of the terms **»intermediary«** and **»fiduciary account«** is provided in amended Article 168 of the LCC-1.). The term »intermediary« is defined based on Directive (EU) 2017/828: an investment firm which, according to Directive 2014/65 /EU is a legal person whose regular activity or business is the professional provision of one or more investment services for third parties and/

or the professional conduct of one or more investment transactions are considered to be intermediaries. In the Slovenian legal system, an investment company is defined in Article 20 of ZTFI-1.

In addition, the requirements of Directive (EU) 2017/828 concerning **directors' remuneration** policy and the greater transparency of **related party transactions** (the Board's obligation to consent to material transactions with related parties is supplemented, as is the obligation to make them public, in the LCC-1 K (Articles 281.b to 281.č). Finally, a **diversity policy** is also introduced and implemented as concerns representation in the management or supervisory bodies of the company from the point of view of gender and other aspects like age, education or professional experience (Article 70).

The amendments to LCC-1 K also affect implementation of Commission Regulation (EU) 2018/1212 establishing minimum requirements for implementing the provisions of Directive 2007/36/EC regarding the **identification of shareholders**, the provision of information, and facilitation of the exercise of shareholders' rights. On this basis, the institutes of asset managers, institutional investors and voting advisers were introduced as a novelty in the LCC-1 K.[28]

28 For more, see: Bohinc, R. Corporations and partnerships, Slovenia.

2. Shareholder Democracy Controversies

2.1 Diverse national legal and policy approaches to shareholder democracy

Key elements of shareholder protection in a certain state, including the main company legislation and the applicable soft law and recommendations, vary substantially among countries, as does the corporate environment**.** The prevailing ownership structure that varies substantially among countries due to **different traditions of law and investment culture** is the biggest reason for shareholders being in a different position and facing inequality in real life. Further, the varying **specific policy requirements and barriers** applied in different states (e.g., for EU non-resident and foreign shareholders) are another cause of inequality in shareholders' positions.

Disparities in national laws (also within the EU) mean that cross-border EU investment or foreign investment is more costly, thereby discouraging such investment. The diverse national approaches to shareholder protection have an impact on cross-border operations**.** These issues make **equity investments by non-resident EU shareholders or foreign shareholders less attractive.** In certain cases, such issues are a particular burden for minority shareholders. The different national approaches to shareholder protection also impact companies' cross-border operations or other company activities (e.g., by **reducing legal certainty, increasing the cost** of legal advice needed to understand the various national systems).

This wide range of national frameworks for the protection offered to shareholders in international (cross-border) cases (regarding both **cross-border equity investment and cross-border trade operations**) considerably affects the position of shareholders in different countries. For instance, the **costs and obstacles faced by minority shareholders** in cross-border versus national cases are therefore higher. A potential investor might even reject the idea due to the diverse shareholder protection barriers or other related restrictions being applied under the relevant national legislation.

There are also big differences between companies **listed** on regulated markets, companies listed on other trading venues, and **non-listed** companies and, where relevant, between public and private companies. Important differences also occur in shareholder protection between listed public limited companies (such as Société Anonyme or Aktiengesellschaft) or non-listed private companies (such as Sarl or GmbH)[29]. Non-listed companies are relevant for minority shareholder protection if they are widely held or dispersed. Non-listed companies may include companies held by a broad group of 'family and friends', or companies which have raised capital through alternative sources of financing but not applied to be listed.

Private companies are very important in a given market, especially when taking the shareholder base and other aspects explained above into account. In some cases, the shareholders of a company itself may be entitled to establish **specific minority shareholder rules** in the company's constitution (statutes, Articles of Association), shareholder agreements etc. Precise arrangements between shareholders could be based on statutory law or case law or be based solely on a business' own particular practice or self-regulation.

Special securities or accounting requirements may apply to **companies operating in certain sectors** (e.g., detailed rules on disclosure and transparency under Capital Requirements Directive IV etc.) or other sector-specific requirements found in existing EU law. In theory (Dallas 2016)[30], even the specific term of **financial firm** as opposed to a **non-financial firm** is in use. A **financial firm** refers to any organisation primarily engaged in lending or investing, regardless of its legal classification (e.g., Limited Partnership, Limited Liability Company, Corporation). The term includes investment and commercial banks, pension funds, mutual funds, hedge funds, structured investment vehicles, and mortgage finance companies.

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29 Company« – **companies that are incorporated as public (**»***public company***«, such as Société Anonyme or Aktiengesellschaft**) or private (**»private company«, such as Société à responsabilité limitée or Gesellschaft mit beschränkter Haftung) **companies limited by shares. *»Listed company*«** **- companies listed on or traded on any trading venues under MiFID operating in the EU, unless otherwise indicated in the text of** the question. Most importantly, trading venues include *»regulated markets«*, but also multilateral trading facilities (MTFs) and, in the future, SME growth markets. Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Directive 2002/92/EC and Directive 2011/61/EU.

30 Dallas, Lynne 10/4/2016, Short-Termism, the Financial Crisis, and Corporate Governance, 37 J. Corp. L. 265, Journal of Corporation Law, Winter 2012.

The position of shareholders in these types of companies is completely different from the position of shareholders in the non-financial sector. Several measures are imposed within the EU to try to overcome these forms of inequality.

2.2 Relativity of the principle of proportionality

The principle of proportionality ('**one share one vote**') means that the proportion of shares in the subscribed capital defines[31] the shareholders' share in the appropriation of profit and the number of voting rights. If contributions to the subscribed capital are not paid in full, or not paid up for all shares in the same proportion, the shareholders' shares in the appropriation of profit are determined according to the payments made.

Shares are individual pieces (units) representing an **equal stake in the subscribed capital** of a Public Limited Company (hereinafter PLC) as the issuer. Shares provide the **legal basis for shareholders' rights**. The total subscribed capital of a company divided by the number of shares is equal to the nominal (face) value or related value of shares, which is the basis for identifying the level of property (appropriation and governance) rights. Yet, **not all shares bring the same rights and shareholders may be in very different positions depending the type of shares they hold. It is hence far from the truth that all shareholders, presumably being partial owners of the company as the issuer of shares, are equal. Shareholders' rights, despite being called property rights, differ from each other substantially depending the kind of share (rights) shareholders have bought or otherwise acquired. The level of shareholders' rights relies on the kind of shares they hold; these rights are however not based on property but on the company–shareholder contractual relationship and the kind of goods (financial instruments) they have bought**.

The holders of **ordinary shares** are entitled to the net profit after the allocation to reserves and payment of preference dividends. If a company winds up, ordinary shareholders are entitled to the assets

31 As in the international accounting standards adopted in accordance with Regulation (EC) No 1606/2002 of the European Parliament and of the Council.

after payment of the debts and of the nominal value of the preference shares. **The holders of preference shares** are eligible for a fixed dividend before a dividend is paid to ordinary shareholders. They are entitled to priority if the company is wound up.

The differences among shareholders concerning their rights continue with the transferability of shares and again depend on which kind of shares (fully or restricted transferable) a shareholder holds. Differences are caused by the PLC issuer (the existing shareholders or the board) or the state (or authorised agency) as the regulator of the securities market. Registered shares may even be compulsory, e.g., for shares that have not been fully paid up. Share certificates must also be in registered form if they are issued prior to full payment of the issue price. The amount of partial payments must be indicated on the share certificate.

Although it is the general principle that each share must confer voting rights, this is not always the reality (treasury shares and shares of the company held by subsidiaries, preferred or preference shares are preferably and normally non-voting). Multiple-voting shares are not permitted, albeit an exception may be granted by a government authority in the public interest.

A share is a transferable security (financial instrument) that enables the circulation of capital on the (organised) financial market (stock exchanges). However, not all shares are a transferable security and the position of shareholders varies here. Transferable shares are offered on a (primary) financial market for sale to raise capital for the company upon its formation or when increasing a PLC's capital and on a secondary market to trade with them. The nominal (face) value, or in the case of non-par value shares the related value of shares, multiplied by the number of shares is equal to the total subscribed capital of a PLC.

The trading of transferable shares is governed by a sophisticated securities market legal framework that puts shareholders in a completely different position compared to the holders of shares that are not publicly traded or even restricted/non-transferable.

2.3 Equitable treatment of all shareholders?

According to the OECD's Principles[32] and majority of national legislations, all shareholders **of the same series** of a class should be treated equally. The corporate governance framework is intended to ensure the **equitable treatment of all shareholders,** including minority and foreign shareholders. All shareholders should have the opportunity to seek **effective redress** for a violation of their rights.

The equitable treatment of all shareholders is obviously limited only to those holding shares of the same series, while otherwise shareholders are definitely not treated equally but depending on the rights they purchased while acquiring their shares. Shares should carry the same rights only within a given series of a class, otherwise different shares would be associated with different rights and that would cause enormous differences (inequality) among shareholders. On the other hand, all investors should be able to obtain information about the rights attached to all series and classes of shares before they make a purchase. Moreover, existing positions of shareholders are extremely rigid; changes in voting rights should be subject to approval by those classes of shares that are negatively affected.

Another way of differentiating shareholders is when such a small number of shares is held that confers no control over the company, and does not meet the minimum criteria for minority shareholders. According to corporate legislations, solely minority shareholders should be protected from abusive actions taken by or in the interest of controlling shareholders acting either directly or indirectly. **Only minority shareholders should have effective means for redress (court action).** The processes and procedures for general shareholder meetings should allow for the equitable treatment of all shareholders.

The basic right of shareholders that should be technically guaranteed for all shareholders equally, depending on the national corporate legislation, includes secure methods for registering ownership (book entry form). In principle, while the right to convey or transfer shares is guaranteed, **legislation permits restrictions**

32 OECD Principles for Corporate Governance, Paris, 2015

or limitations imposed by articles of incorporation that place shareholders in uneven positions.

The right to obtain relevant and material information on the corporation on a timely and regular basis is safeguarded and even protected by court action does not depend on the type or number of shares and thus shareholders undisputedly enjoy equitable treatment. The most fundamental rights to vote at general shareholder meetings, to elect and remove members of the board, and the right to a share in the profits of the corporation are enjoyed depending chiefly on the type and, of course, the number of shares.

Shareholders are not supposed to run the company, despite having invested their money in it. This is the responsibility of corporate boards. Still, by exercising the right to vote at the general meeting shareholders decide on certain fundamental issues. **Following the principle of proportionality and equality, shareholders have a right and duty to decide upon the issues most relevant to the company, namely**:

– the approval of the **distribution of profits;**
– the **election of board members**, and/or key **executive compensation;**
– the approval and amending of the **company's basic documents** (articles of association, statute);
– the approval of **extraordinary transactions** (mergers, divisions, conversions, alteration of capital, corporate contracts, dissolution);
– the **issue of additional shares by increasing the capital** and excluding the priority right of existing shareholders to buy the new shares issued;
– the approval or election of **auditors;**
– the direct nomination of board members; and
– the approval of material **related party transactions**.

The most fundamental decisions of the company are left to all shareholders, including those who have just acquired their shares and have no idea of the company's performance whatsoever. The success of the power play between shareholders and managers depends on the concentration of ownership: the more the ownership is concentrated, the greater the shareholder activism and the smaller the power that is left to the managers (for the concentration of ownership, see the separate chapter).

Those employed by the company bear the risk of losing their jobs, yet do not decide on any matters; they even do not help to elect the board that determines their destinies. Employees also do not enjoy ex-ante rights like minority shareholders do (e.g., placing items on the agenda of the shareholders' meeting), nor ex-post rights (to seek redress once rights have been violated in shareholder court actions).

2.4 The general meeting of shareholders

The Shareholders Directive 2007/36 establishes several requirements in relation to convocation of the general meeting. The company (**its board**) issues the convocation of the general meeting (no later than on the 21st day before the date of the meeting). **Employees have no influence on convocation of the general meeting of shareholders.** The convocation rules are very precise when it comes to safeguarding the position of shareholders. The notice of convocation must at least indicate precisely when and where the general meeting is to take place, and the proposed agenda. The convocation contains a clear and accurate description of the procedures that shareholders must comply with to be able to participate and to cast their vote at the general meeting. An explanation must be provided that only those who are shareholders on the notified date have the right to participate and vote at the general meeting, along with an indication of where and how the full text of the documents and draft resolutions can be obtained and the address of the Internet site at which the information is available.

Shareholders acting individually or collectively have the right to put items on the agenda of the general meeting and to table draft resolutions if each item is accompanied by a justification or if there is right to draft a resolution. According to company legislation (EU Directive 2007/36 on certain rights of shareholders) and recommendations (the OECD's Principles), shareholders should have the opportunity to participate effectively and vote at shareholder meetings and to be informed of the rules that govern shareholder meetings, including the voting procedures. Shareholders should be furnished with sufficient and timely information concerning the date, location and agenda of general meetings, and regarding the issues to be decided at the meeting. Shareholders should also be informed about the processes and procedures for shareholder meetings and the principle of equitable treatment of all shareholders. Company procedures should not make it difficult or expensive to cast votes. **None of these rights is conferred on the employees. Employees (at least their representative) are also not invited to the general meeting, nor do they have any rights to cast votes.**

Shareholders should have the opportunity to ask questions to the board and propose items for the agenda and resolutions of the shareholders' meeting. It should also be possible for shareholders to ask questions about the external auditor's report (OECD Principles). Shareholder resolutions to be placed on the agenda must be supported by shareholders holding a specified percentage of shares or voting rights (5%, 10%). This threshold should be determined taking the degree of ownership concentration (OECD Principles) into account. Effective shareholder participation in key corporate governance decisions, such as the nomination and election of board members, should be facilitated. Electing members of the board is a basic shareholder right. Shareholders should be able to participate in the nomination of board members and to vote on individual nominees or different lists of them (OECD Principles).

However, employees are given none of these possibilities. Employees have no tools available to acquire information at the general meeting about the performance of the company or their position, except for those imposed by some countries in the context of participatory regulation (industrial democracy, co-determination) or voluntarily conferred by the shareholders. At a shareholders' meeting, the company's management must provide the shareholders with reliable data concerning company matters to help evaluate the agenda items. Under Directive 32/2007, every shareholder **(but no employee)** has the right to ask questions about items on the agenda of the general meeting; the company must answer the questions put to it by the shareholders.

Legislation around the world generally permits voting by proxy. Every shareholder has the right to appoint any other natural or legal person as a proxy holder to attend and vote at a general meeting in their name. The proxy holder enjoys the same rights to speak and ask questions at the general meeting. **Proxies should vote according to the instructions of the proxy holder, yet in reality this does always happen**. This is the reason for the important changes made concerning disclosures by proxies, that we discuss in a separate chapter. Already before these changes, the OECD's Principles, recommended that the instructions for voting should be disclosed where proxies are held by the board or the management for company pension funds and for ESOP.

EU Member States have quite different legislation on proxies in place and this influences the varying positions of shareholders here. Some states limit the appointment of a proxy holder to a single meeting or to such meetings as may be held within a given period and the number of persons a shareholder may appoint as proxy holders in relation to any one general meeting.

2.5 Shareholder democracy as property democracy rather than people's democracy

Ownership structure refers to the distribution of shares held by individual shareholders of a company. Shareholders normally differ in their size expressed as the number of shares (percentage of equity) they hold in a certain company: from small shareholders to large block shareholders. Although there is no legal definition of either types; investors holding at least 5% of equity ownership are in theory already considered to be a block holder. Block holders are often an institutional investor (pension funds, investment companies, mutual funds).

Due to holding different numbers of shares and respecting the 'one share one vote' principle, shareholders' power to govern the corporation is by definition unequal when the majority principle is respected as a basic principle of shareholder democracy. Inequality among shareholders creates the grounds for conflicts and coalitions and some of them eventually win and control the corporation, leaving the rest powerless and without rights. This is how shareholder democracy based on the 'one share one vote' and majority principles works in real life.

Shareholder democracy[33] is in fact the key reason for inequality among individuals holding shares in terms of their power to affect the company's governance. Property rights are namely attached to shares rather than to the people holding them. Only the shares are

33 See: Shareholder democracy and the curious turn toward board primacy, Hayden, G., & Bodie, M. T. (2009). Wm. & Mary L. Rev., 51, 2071.

relevant for distribution of power to run and to make profit from the company. Here we may talk of a property-owing democracy rather than a people's democracy.

Cyclical crises are caused by the fact that the big ones, with all the power they possess under the rules of shareholder democracy, do not perform their tasks and duties well. They do not sufficiently engage, follow short-term profits, act opaquely, and are led by individual greed rather than general well-being. These motivational bases bring the development wheel to a cyclical stop and threaten the existential position of the masses of the other stakeholders who have no social power. Distribution of the decision-making power exclusively by the number of shares allows the minority overfull elite by socially irresponsible behaviour to cause social distress to the powerless majority..[34]

2.6 Ownership concentration as an internal governance mechanism

A company's ownership structure (concentrated or dispersed) substantially affects the possibilities of implementing individual shareholders' corporate rights. Block holders (shareholders with a significant number of shares) may have incentives to proactively safeguard their investment may even (directly or indirectly) take aggressive action over firm decisions like the election of board members and replacement of management with their voting power. Sufficient ownership concentration is an individual shareholder goal per se since it ensures control over the company's decisions.

Ownership concentration is used as an internal governance mechanism to help reduce the possibility of managerial opportunism because managers and boards of directors are more likely to take the preferences and interests of large shareholders into account.[35.]

34 See: Rawls, J. (1999), A Theory of Justice, revised edition, Cambridge/MA (2001), Justice as Fairness, E. Kelly (ed.), Cambridge/MA, (2005), Political Liberalism, expanded edition, New York, (2007), Lectures on the History of Political Philosophy, Cambridge/MA

35 http://lexicon.ft.com/Term?term=ownership-concentration

Namely, ownership concentration is an internal governance mechanism that allows owners to influence the management of the firm to protect their interests. **Yet, at the same time ownership concentration leads to shareholder activism, which means short-termism in the maximisation of profits is a major explanation for a company's inefficient and poor business performance in the long run. Companies with a low level of ownership concentration (highly dispersed shareholders) are normally left to be run by professionals (managers or managerial boards) rather than shareholders, which qualifies them to be more competitive and successful.** By contrast, firms with a low level of ownership concentration (diffused ownership) might indicate weaker governance power because investors with smaller ownership interests have little incentive to pay attention to the firm's strategic decisions and are thus less motivated to closely monitor and discipline the behaviour of top executives. Compared to large block holders, small investors are more likely to 'vote with their feet' when the firm performs poorly.[36]

Conceptually, although concentrated ownership may improve performance by increasing monitoring and alleviating the free-rider problem in takeovers, other mechanisms may work in the opposite direction. Frequently discussed is the possibility that large shareholders exercise their control rights to create private benefits, sometimes expropriating the returns to smaller investors.[37] **Here we are talking about related party transactions and excessive remuneration.** One study shows that firms from the high-technology sector have a lower ownership concentration than firms in more 'mature' industries.[38]

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36 Ibid.

37 Ownership Concentration and Corporate Performance on the Budapest Stock Exchange: Do
Too Many Cooks Spoil the Goulash? John S. Earle *W. E. Upjohn Institute*, Csaba Kucsera, *Hungarian Academy of Sciences*, Álmos Telegdy, *Budapest University of Economic Sciences,* Upjohn Institute Working Paper No. 03–93, 2004.

38 Ownership Concentration and Firm Performance: Evidence from an Emerging Market, William Davidson Institute Working Paper No. 834, 27 Pages Posted: 17 Aug 2006.

2.7 Ownership structure and equality among shareholders

The fundamental problem of a contemporary shareholder democracy is reducing **the conflicts of interest between dispersed small shareowners and powerful controlling shareholdings.** Research[39] shows that huge and **influential voting blocs foster the activism of shareholders,** often leading to short-termism, which becomes a decisive corporate governance vehicle, with all of its inefficiencies, **that depresses securities market competition and squeezes minority shareholders out**.

The effects of countries' ownership structure and securities market regulation on the performance of an economy are considerable. Securities market regulation affects the creation of the ownership structure to an important extent, and vice versa. Both securities market regulation and ownership structure therefore affect the position of shareholders in very different investment and governance environments.

Ownership structure research in EU countries shows a **high degree of concentration of shareholder voting power in continental Europe** relative to the USA and the UK. However, the position of large controlling shareholders is completely different than that of weak minority shareholders, **even though both groups have the same rights and operate under the principle of equality.**

If shareholders conclude a **shareholders' or voting agreement, they become even more concentrated and stronger compared to the other shareholders.**[40] Huge and influential voting blocs foster

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39 Dallas, Lynne 10/4/2016, Short-Termism, the Financial Crisis, and Corporate Governance, 37 J. Corp. L. 265, Journal of Corporation Law, Winter.

40 Becht, Marco, Ailsa Roell, European Economic Review 43 (1999) 1049/1056, Corporate Governance in Europe, Block holdings in Europe: An international comparison:
»The rarities are mainly the large blocks held by Berkshire Hathaway. Even with their weaker holdings, some institutions have been active, seeking to elect directors, making shareholder proposals, petitioning the SEC to loosen constraints on their activity. Aggregate concentration already makes the U.S. look like a pale comparison of its foreign counterparts. The top twenty-five institutional investors on average vote 16% of the stock of the largest twenty-five U.S. corporations. While U.S. concentration trends tended to slow down in the early 1990s, and the U.S. concentration is a far cry from

shareholders' activism that even strengthens strong shareholders and weakens the other shareholders; this is becoming a decisive corporate governance vehicle, together with having an important impact on competition in the capital market.

Obviously, the issue of shareholders' equality in the capital market cannot be solved by the contractual approach. What is needed here are mandatory corporate and securities market rules to protect minority shareholders and securities market competition. Rules on the securities market only (e.g., disclosure requirements and the prohibition on insider trading) and on tax obviously cannot prevent ownership concentration leading to financial monopolies, in the terms of huge voting blocs being formed that depress minority shareholders, and to short-termism and monopolies in the securities market. More rigorous and stricter compulsory corporate law rules are needed to overcome the inequalities embodied in the monopolised securities market.

2.8 The separation of ownership from control

Classic works like those by Berle and Means (The Corporation and the Private Property, 1932) and Jensen and Meckling (1976) pointed to the separation of ownership and control and its consequences. They demonstrated that shareholders exercise virtually no control over either day-to-day operations or long-term policy of the company. Instead, control is vested in the hands of professional managers, who typically own only a small portion of the firm's shares or none at all.

Under both company law (EU and US) and company statutes (articles of incorporation), the key players in the formal decision-making structure are members of the board of directors[41]. **The Board of Directors and executive managers acting alone**

the five banks in Japan that vote 20% of the stock, or the three German banks that vote 40%, large firm ownership is no longer that of an atomised Berle-Means corporation«.

41 As §141(a) of the Delaware General Corporation Law states, the corporation's business and affairs »shall be managed by or under the direction of a Board of Directors«.

accordingly make the vast majority of corporate operational decisions. Shareholders essentially have no power to initiate corporate action and are entitled to approve or disapprove only a very limited number of board actions. Although the company law concept (legislative framework for director's duties and liabilities) does not provide a basis for shareholder activism, it also does not successfully prevent it. Shareholder activism as a decision-making process in concentrated ownership companies is not even expressly legally prohibited.

In real life, **concentrated ownership** normally (but not necessarily) also means concentrated voting power, which causes strong shareholders' incentives regarding management and, as a consequence, weak managers (board of directors). The presence of strong majority owners makes minority owners as well as the managers weak. This is the optimal setting for shareholder activism. Shareholders not included in the controlling package have no control, despite having a 49% share of the company. The separation of ownership from control is expressed for shareholders outside of the controlling package. Yet, in the case of **dispersed ownership**, it is quite the opposite: the voting power is also dispersed with the typical outcome that the managers are strong and the owners are weak. The separation of ownership from control is particularly evident.

However, business life rarely follows pure theoretical models. With the application of voting rights restrictions (non-voting shares), **concentrated ownership might not simultaneously mean concentrated voting power,** but keep it dispersed. Once again, this means strong managers and weak owners and a pronounced separation of ownership from control. And the opposite, **dispersed ownership can still lead to concentrated voting power** if certain devices are used, such as: voting trusts, hierarchical groups, non-voting shares, voting pacts, minority voting blocs, and soliciting proxy votes. This makes managers weak again because of the presence of strong voting blocs.[42]

[42] For more, see: Marco Becht, Strong Blockholders, Weak Owners and the Need for European Mandatory Disclosure, European Corporate Governance Network, Executive Report Last Revised: 27 October, 1997, (hereinafter: Becht, 97).

In some countries (Germany, Slovenia), voting rights can be restricted by the articles irrespective of the number of total votes held. For example, where an individual can own up to 30% of the votes in a corporation but the articles allow them to a maximum of 5% of the vote. If everybody else owns 5% voting blocs, the ownership is more concentrated than the voting power.

2.9 High concentration in the EU and considerable dispersion in the USA and the UK

The ownership structure in continental EU countries early in the millennium stood out for the high level of concentration (Enriques, Volpin, 2007)43 while, according to Roe, institutions owned just 8% of the stock of the largest American firms in 1950 but in the **1990s they only owned half**, albeit in small, un-concentrated blocs. The five biggest holders rarely together own much more than 5% of the largest US firms (Roe, 1994). In several EU countries, the median largest voting stake in listed companies exceeds 50%; voting control by a large block holder is the rule more than the exception**.** Empirical studies show that ownership is highly concentrated in Germany and Italy, and diffused in Britain and America, with France in an intermediate position. Remarkably, in half of all German and Italian listed companies a single block holder owns at least 57% or 55%, respectively, of the votes[44].

The votes of shareholders who are not part of the controlling (voting) bloc (51% or even 75%) do not count at all despite them formally enjoying all property rights attached to the shares and participating in all decision-making procedures. As we have already discovered, concentrated ownership (voting power) **weakens the position of managers and empowers the direct**

43 The European Commission's 1988 Transparency Directive requires Member States to enact laws directing the shareholders of companies listed on a member state exchange to notify the relevant authorities and the company itself within 7 days whenever their voting rights cross the thresholds of 10%, 20%, 1/3 (or 25%), 50% and 2/3 (or 75%).

44 Corporate Governance Reforms in Continental Europe, Luca Enriques and PaoloVolpin, Journal of Economic Perspectives, Volume 21, Number 1, Winter 2007, pp. 117–140.

influence of block shareholders. The risk of managers acquiring private benefits is less expressed, although the danger of squeezing out the other shareholders is greater.

The European type of shareholder activism can thus potentially arise (in Europe, 'shareholder activism' refers to small shareholders defending their interests against controlling block holders), rather than the US type (in both the USA and the UK, 'shareholder activism' refers to the increased monitoring of managers by weak shareholders).

Rather than protecting shareholders against the management, the main policy objective of legislation (*ratio legis*) should be **protection of the other shareholders from being squeezing out** by block holders. The monitoring of managerial performance from the point of view of a bloc of shareholders is presumably not a legal problem given that the bloc is composed of active (institutional) shareholders. Yet, the problem of an influential block holding being disinterested in the behaviour of the corporation's management remains, as does the problem of independent management. These problems cannot simply be solved by leaving management and shareholders' blocs to make an agreement and while leaving the other shareholders to resolve their problems through court actions.

Legal regulation of the **securities market can strongly affect how the dispersion of ownership** impacts the concentration of monopoly powers and prevent the forming of huge block holdings and voting pools with all the negative implications for corporate governance efficiency and fair competition in the securities market. The legal regulation of the securities market, especially the issues of the requirement of full disclosure, mandatory takeover bids, rules and regulation on fair dealings, insider trading prohibitions, together with the tax regulation of the transfer of shares within a short period can contribute to fair competitiveness in the securities market as a prerequisite for efficient corporate governance and the protection of the rights of minority shareholders.

2.10 Reasons for institutional ownership prevailing and employee ownership disappearing

According to the EFES[45] database for 2017, a controlling shareholder (a single person holding at least 25%) can be detected in 57% of all large European listed companies (42% of the whole stock capitalisation). Eight categories of controlling shareholders are identified: **Executive, private investor, family, foundation, corporation, founders, state, and employees.** The 'democratisation rate' is calculated as the **percentage of employee shareholders amongst all employees.** Generally speaking, the existence of a controlling shareholder is a negative factor for employee share ownership. There are two exceptions: employee share ownership is more developed in state-controlled companies, and the highest democratisation rate (87.4%) can be observed when employees are the controlling owner. When the controlling shareholder is an executive director, the democratisation rate of employee share ownership is only 7%. It is also low, ranging from 12% to 14%, when the controlling shareholder is a private investor or fund, a foundation, a family, or the founder of the company. In this sense, 'negative' ownership control can be seen in companies where an executive director, private investor, founder, family or foundation is the controlling shareholder, whereas 'positive' control corresponds to companies without any controlling shareholder or when the state or the employees are the controlling shareholder.

The same holds for many post-transitional countries where blocs are made up of institutional shareholders, having obtained their shares *ex lege* primarily through the privatisation process. Former countries in transition with prevailing state or social ownership namely underwent a demanding process of privatisation and the legal restructuring of state and partly state-owned companies. It is paradoxical that, despite privatisation, state and municipal holdings and funds such as investment companies, state-owned banks and

45 The information in the EFES database is practically exhaustive with respect to European listed companies, knowing that the 2,402 listed companies in the database represent 25% of all European listed companies (excluding asset management, investment funds and real estate funds), but 99% of the whole stock capitalisation and 96% in terms of employment.

insurance companies today still hold over 50% of the shares in a considerable number of companies.

The dominating institutional ownership structure in terms of size and especially political influence on decision-making is very typical for post-privatisation countries economies. The State as an active professional owner, particularly in industrial branches of public interest where it combines and mostly combines its position as owner with those of authority and regulator. This frequently makes corporate decisions dependent on political goals, including the goals of political parties that control a given field.

In former countries in transition, internal (employee) ownership does not work well and has been decreasing since privatisation. Banks, brokerage firms and trusts, nor management, as potential proxies, do not usually organise diffused (minority) shareholders. In some places, they organise themselves by way of different 'shareholders' associations' that occasionally protect the interests of minority shareholders' quite effectively.

While in some places employee shareholders impose their influence on the company via special trusts or cooperatives, this is rare in countries in post-transition because these concepts are not sufficiently tax stimulated; their ownership stake has been shrinking substantially since the privatisation process was completed. Individual employee shareholders, who still persist, do not actually attend the shareholders' meeting nor participate as individuals or groups in dialogue among the shareholders, while also not having developed any relationship with the supervisory and even less the management boards.

Shareholder democracy is not intended for small shareholders like employees. With shareholder democracy, only the big who enjoy majority rule take power, prosper and win. Accordingly, the shareholding of employees, as small shareholders, disappears wherever there are no mechanisms in place for their equal treatment (like ESOP) and so long as there are no tax incentives for the big ones to open the way for employee ownership.

3. Conclusion

Corporate governance around the world and is far from being harmonious. Despite growing convergence in various areas, convergence or divergence continues to be a permanent dilemma with EU company law.

The most fundamental decisions of a company are left to all the shareholders. Employees, however, neither enjoy ex-ante rights, like minority shareholders do (e.g., placing items on the agenda of the shareholders' meeting), nor ex-post rights (to seek redress once rights have been violated in shareholders' court actions).

Property rights are attached to shares rather than to the individuals holding them (property democracy rather than people's democracy). Ownership concentration leads to shareholder activism that causes short-termism in the maximisation of profits to be one of the biggest explanations for inefficient and poor business performance.

Although the company law concept (legislative framework for directors' duties and liabilities) does not provide a basis for shareholder activism, it also does not successfully prevent it. Shareholder activism and managerial short-sightedness (myopia) as the decision-making in process concentrated ownership companies is not even expressly legally prohibited.

The votes of shareholders who are not part of the controlling (voting) bloc (51% or even 75%) do not count at all despite them formally enjoying all the attached property rights and participating in all decision-making procedures.

Shareholder democracy is not intended for small shareholders like employees. With shareholder democracy, only the big who enjoy majority rule take power, prosper and win. This is leading to the disappearance of the shareholdings of employees as small shareholders.

Disregarding the structural measures designed to strengthen the position of employees whose long-term stability is of the greatest natural interest is a huge shortcoming of all anti-short-terminist measures, with the causes of this lying in the ideological systemic exclusion of employees from decision-making.

While several measures have been imposed in the EU in an attempt to overcome these shortcomings, no measure involves those who are most interested in the corporation's long-term success because their existence depends on it, i.e., the employees, not in the EU's measures, nor those of the OECD. The ideological barriers are too great.

The constant and numerous amendments to corporate legislation in Slovenia are generally due to following and implementing the EU's corporate regulations. This means that there are no original and innovative solutions based on national peculiarities and traditions.

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IS STRONGER SHAREHOLDER ENGAGEMENT TRULY ALL WE NEED?

Rado Bohinc

Abstract

In this article, we aim to answer questions about the causes, consequences and ways of eliminating the most current and practically expressed shortcomings of corporate governance best known as: shareholder activism, short-termism, and managerial short-sightedness (myopia).

It is obvious that as an important goal we can only stimulate, rather than force, owners (investors) and managers to act responsibly, thoughtfully and patiently, taking the long-term benefits of the corporation and its employees into account, including the latter's job security.

Patience and long-term responsibility for the company's development are generally not part of managerial culture and business behaviour. Accordingly, the law should, at least to some extent, enforce responsible business behaviour and sustainability.

In this article, we seek to determine efficient ways of strengthening the position held by shareholders and find incentives for their long-term business and development orientation and responsibility. We also present measures introduced by the EU and the OECD to overcome managerial and investors' short-sightedness along with their implementation. We ask, whether short-termism among investors and managerial short-sightedness can be overcome without including the interests of employees and other stakeholders in management decisions concerning business and development.

Key words: short-termism, shareholder activism, managerial short-sightedness (myopia), shortcomings of corporate governance, shareholders' engagement, employee involvement

1. Introduction

The biggest shortcomings of contemporary corporate governance according to EU Directive 2017/828 include: short-termism, managerial short-sightedness (myopia), and the lack of transparency and any greater shareholder involvement. The insufficient involvement of stakeholders (employees) is not considered to be a systemic corporate governance problem in the Directive.

The EU has imposed several measures to try to overcome shortcomings such as the inadequate engagement of institutional investors and asset managers and the missing transparency of proxy advisors. These measures generally relate to overcoming short-termism and improving the quality of shareholder decision-making, especially in the relationship between the intermediaries of institutional owners and asset managers.

The aim of Directive 2017/828 is limited to facilitating interaction between companies and shareholders, a more long-term focus in corporate governance, and shareholders becoming more involved in corporate governance as a way of improving companies' performance. The right of companies to identify their shareholders is imposed while the exercise of shareholders' rights through intermediaries is more strictly regulated, especially as concerns institutional investors, asset managers and proxy advisors

Still, no corporate governance reform measure tackles the position held by employees and other stakeholders in corporate governance. Directive 2017/828 does not address the shortcomings related to the lack of cooperation with stakeholders in a company's decision-making.

It is clear that all fundamental decisions of a company are left to the shareholders, including those who may have just acquired their shares and have no idea about the company's performance whatsoever. Employees, in contrast, enjoy neither ex-ante rights like minority shareholders do (e.g., placing items on the agenda of the shareholders meeting), nor ex-post rights (redress for after when rights have been violated, shareholders' court actions).

Measures to involve those most interested in the corporation's long-term success because their existence depends on it, i.e., the employees, have yet to be proposed to overcome corporate governance shortcomings in the EU regulation or in the OECD recommendations. The ideological barriers are simply too great.

2. The Main Corporate Governance Shortcomings

2.1 Shareholder activism and managerial short-sightedness (myopia) as a central issue in modern corporate governance

Effective shareholder engagement has been placed in the centre of the battle to eradicate the causes of the cyclical financial crisis. Indeed, in recent decades corporate investors have shown a tendency to disregard the due exercise of their rights by focusing exclusively on short-term results.

Corporate theory discusses the short-sightedness of managers in the context of the classical theory of agency costs. Dallas 2016 states that, unlike the well-known agency cost theory, which holds that agency costs are minimised when managers are disciplined by market pressures, such as through hostile takeovers or managerial compensation tied to stock prices, managerial myopia theories explain why **managers »caring too much« about current stock prices** leads to myopic decision-making.

If the share price of a company's stock is undervalued, **managers may act myopically to signal positive information to the market**, such as inflated current earnings, in an attempt to raise the price of the company's current stock price. The fear of a takeover due to the company having an undervalued stock price may lead managers to focus more on short-term profits than on long-term objectives (Stein J. 1989).

Short-termism is the obsession of investors, asset management firms, and corporate managers with short-term results. Dallas 2016 describes how short-termism is embodied in the corporate governance concept based on the agency cost principle and related **exclusion of employees from decision-making** concerning the management of a corporation.

Structural **measures to strengthen the position of employees,** whose long-term stability is of their highest natural interest since they and their families depend on it, **are absent**. Disregard of this circumstance is one of the huge shortcomings of all the anti-short-termism measures in the conduct of management and shareholders. Unfortunately, this absence of measures concerning employee participation has its origins in the ideological systemic exclusion of employees from decision-making and corporate governance.

Dallas (2016) sees short-termism and short-sightedness (myopia) not as a random or cyclical repetitive mistake, but as a **systemic (structural) weakness of corporate governance** based exclusively on the principal–agent relationship, and which by definition exclude employees of the management despite them being vitally interested in the long-term life of the corporation.

According to the Centre for Financial Market Integrity (CFMI) and the Business Roundtable Institute for Corporate Ethics (CFI), short-termism collectively brings the **unintended consequences of destroying long-term value**, lowering market efficiency, reducing investment returns, and impeding efforts to strengthen corporate governance[1].

The CFI recommends that corporate leaders, asset managers, investors, and analysts reform earnings guidance practices, develop long-term incentives across the board, structure compensation for corporate executives and asset managers so as to achieve long-term strategic and value-creation goals and to demonstrate leadership in shifting the **focus to long-term value creation**. Improving communications and transparency and promoting the broad education of all market participants about the **benefits of long-term thinking** and the costs of short-term thinking[2] are also recommend by the CFI.

As may be seen, theory and expertise assert that a company's long-term orientation can be promoted and achieved in ways other than strengthening the position of shareholders. This means it is necessary to concentrate largely on the **motivational factors objectively followed by managers**. The long-term orientation of a company would be strengthened considerably by ensuring the **greater**

1 Breaking the Short-Term Cycle, Discussion and Recommendations on How Corporate Leaders, Asset Managers, Investors, and Analysts Can Refocus on Long-Term Value, Proceedings of the CFA Centre for Financial Market Integrity and the Business Roundtable Institute for Corporate Ethics. Symposium Series on Short-Termism

2 Ibidem

inclusion in management decision-making regarding employees' interests, which are no doubt the most long-term since they are connected to their life career paths.

2.2 Short-termism as a structural problem of financial capitalism

If we view short-termism as a **structural problem of financial capitalism**, which is the extreme level of the neoliberal economic model, it becomes obvious that mere recommendations made by professional organisations cannot be a sufficiently effective measure for overcoming the fundamental causes of the cyclical financial crisis.

Magalhães Correia (2014) believes the financial crisis of 2008 exposed the drawbacks of stakeholder activism based on short-term approaches. Indeed, shareholder short-termism has proven to encourage companies to incur unnecessary risks and overlook long-term consequences, with **potential systemic effects for financial markets**.

Dallas (2016) contends that the financial crisis of 2007–2009 was preceded by a period when **financial firms were seeking short-term profits** regardless of the long-term consequences. Numerous market participants engaged in myopic behaviour, including mortgage originators, securitisers, credit default-swap sellers, rating agencies, and investors.

According to Dallas (2016), short-termism (or myopia) is defined as the **excessive focus of corporate managers, asset managers, investors**, and analysts on short-term results, whether quarterly earnings or short-term portfolio returns, and letting go of the concern for firms' long-term value creation and fundamental value.

As Dallas (2016) claims, evidence showing that short-term trading by transient institutional investors leads to **earnings management and that short-termism** is pervasive in the business community, causing long-term damage to both financial and non-financial firms. Dallas (2016) states that this points to the need to re-examine direct methods for discouraging short-term trading; an **excise tax on securities transactions**, including stock, debt and derivatives, would create incentives for long-term investments and also provide resources for a fund used to address the negative consequences of short-term trading. **Modifying capital gains and loss taxation** and repealing mutual fund rules that require quick redemptions are also recommended to discourage short-term trading (Dallas 2016)**.**

There are some other **structural recommendations** that Dallas (2016) proposes to mitigate short-termism:

– the use, or threatened use, of voting rights by short-term traders to pressure firms to engage in short-termism;
– excluding from voting those shares that are hedged to prevent voting inimical to the best interests of the firm;
– imposing fiduciary duties on a broader range of market professionals, that in turn also have an impact by changing the institutional setting in which they operate and the roles that they themselves perceive as playing;
– requiring the unwinding of share ownership over a period of years, or tax incentives for so doing; and
– to base a substantial portion of the managers' compensation on the long-term health of their firms.

In addition, a **dual board structure** (as distinct from the German two-tiered board structure) is proposed to ensure greater board accountability and to counter the trend of the stronger centralisation of managerial power in CEOs, which leads to less CEO accountability (Dallas 2016).

2.3 Insufficient engagement of institutional investors and asset managers

Shares of equity investments can be held by institutional investors like mutual funds, pension funds, insurance companies, and hedge funds. The ability and interest of institutional investors and asset managers to engage in corporate governance varies widely. Some of them are **insufficiently engaged, follow short-term profits,** or are led by individual interests rather than by the shareholders they represent.

Engaging shareholders means that shareholders (especially institutional investors, asset managers and proxy advisors) should be encouraged to engage more in corporate governance and that shareholders should oversee the remuneration policy, related party transactions, and the cooperation of shareholders.

According to the EU **key corporate governance shortcomings** concerned with the behaviour of companies, their boards and shareholders (institutional investors, asset managers, intermediaries, proxy advisors) are the insufficient engagement of institutional investors and asset managers and the inadequate transparency of proxy advisors. In addition, there is an **insufficient link between directors' pay and their performance** and a lack of shareholder oversight of related party transactions[3].

Long-term, responsible and active shareholder engagement would contribute to a significant **improvement in companies' performance, profitability and efficiency**. While long-term commitments (holding on to shares for longer) would provide more long-term capital to companies, their short-term orientation does not permit this.

The EC has made several proposals for the financial sector[4], many of which have been adopted, to improve corporate governance[5]; for

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3 EC Communication of 2003 - Modernising Company Law and enhancing Corporate Governance in the EU - A Plan to Move Forward (2003 COM (2003) 284 final COMMUNICATION FROM THE COMMISSION TO THE COUNCIL AND THE EUROPEAN PARLIAMENT, Modernising Company Law and Enhancing Corporate Governance in the European Union - A Plan to Move Forward deals with the issue of **enhancing shareholders' rights in listed companies** and the problems relating to **cross border voting**. EP Resolution of 2004, expresses its support for the Commission's intention to **strengthen shareholders' rights**, in particular through the extension of the rules on **transparency in proxy voting**, through the possibility of participating in general meetings **via electronic means** and ensuring that cross-border voting rights are able to be exercised

4 In December 2010, the Basel Committee issued detailed rules of new global regulatory standards on bank capital adequacy and liquidity that collectively are referred to as Basel III. The Basel Committee on Banking Supervision (BCBS) has the task of developing international minimum standards on bank capital adequacy. Following the financial crisis, the Basel Committee has reviewed its capital adequacy standards. Basel III is the outcome of that review.

5 See: Regulation of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012 and Directive of 26 June 2013, on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC (referred as Capital Requirements Directive)

instance, on the functioning of boards, risk management, and the remuneration of risk-takers in financial institutions[6].

There is a lack of implementation of the OECD Principles while the corporate governance framework should provide both **sound incentives throughout the investment chain** (long and complex, with numerous intermediaries standing between the ultimate beneficiary and the company) and for stock markets to function in a way that contributes to good corporate governance.

2. 4 The lack of transparency

Companies need to provide **better information** about their corporate governance **to their investors** (shareholders) and society (broad public). Investors should become more transparent about their voting policies so that a more fruitful dialogue on corporate governance matters can take place. More transparency is needed in the relationship between the company and its shareholders, other stakeholders and the broader public as well. Companies should be allowed to know **who their shareholders are.**

The OECD Principles also recommend that **institutional investors disclose their policies** with respect to corporate governance; they should have direct contact and dialogue with the board and management.

Following the 2012 Action plan, the revised Shareholder Directive (EU) 2017/828 tackles corporate governance shortcomings associated with listed companies and their boards and shareholders (institutional investors, asset managers, intermediaries and proxy advisors). This helps to **ensure that shareholders engage more** and manage the company better to act in the company's long-term interests[7].

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6 2010 Green Paper on corporate governance in financial institutions (IP/10/656 and MEMO/10/229, 2011 Green Paper on the EU corporate governance framework (IP/11/404), 2013 Green Paper on the long-term financing of the EU economy (IP/13/274)

7 The Commission already in 2010 launched a Green Paper on corporate governance in financial institutions and, in 2011 it proposed stricter rules on corporate governance in financial institutions in the framework of the CRD IV package.

A long-term perspective creates better operating conditions for listed companies and adds to their competitiveness. This includes stronger transparency requirements for institutional investors and asset managers in their investment and engagement policies regarding the companies they invest in, as well as a framework to identify shareholders to allow them to more easily exercise their (e.g., voting) rights. **Proxy advisors must also become more transparent** about the methodologies they rely on to prepare their voting recommendations and how they manage conflicts of interest[8].

Moreover, Agenda 2020 from 2010 requires a **modern and efficient corporate governance** framework for European undertakings, investors and employees; it must be adapted to the needs of modern society and to the changing economic environment. The EP's Resolution of 2012 highlighted the importance of corporate governance for society, expressing its view on the questions raised by the 2011 Action Plan. Directive 2017/828 of 17 May 2017, amending Directive 2007/36/EC as regards the encouragement of long-term shareholder engagement, aims to improve shareholders' engagement, increase control over directors' remuneration and restrain transactions with related parties.

2.5 Shareholders' greater involvement to improve company performance

The EC's measures **encourage shareholders to engage more strongly** with the companies they invest in, and take a longer-term view on their investment. To this end, they need to have rights to exercise proper control over the management. The answer to this corporate governance shortcoming was **Directive 2017/828 on long-term shareholder engagement**[9].

The biggest shortcomings according to this Directive are: short-termism, insufficient oversight of directors' pay and related party

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8 European Commission proposes to strengthen shareholder engagement and introduce a »say on pay« for Europe's largest companies. http://europa.eu/rapid/press-release_IP-14-396_en.htm?locale=en

9 Directive (EU) 2017/828 of 17 May 2017 amending Directive 2007/36/EC (also The directive 2017/828 on long-term shareholder engagement).

transactions in interactions between companies, and shareholders not being effective in cross-border situations. **The lack of the cooperation or inclusion of stakeholders is not included among the shortcomings in Directive 2017/828.**

As concerns long-term shareholder engagement, Directive 2017/828 prescribes obligations for:

- **intermediaries;**
- **institutional investors** (undertakings carrying out activities of life assurance and of reinsurance, mutual funds, pension funds, hedge funds);
- **asset managers** (investment firms that provide portfolio management services to investors);
- **alternative investment fund managers,** management companies or investment companies; and
- **proxy advisors** (a legal person that on a professional and commercial basis analyses the corporate disclosure and, where relevant, other information of listed companies with a view to informing investors' voting decisions by providing research, advice or voting recommendations that concern the exercise of voting rights).

The aim of the Directive is to improve the engagement in identifying the shareholders, disclosing information, the exercise of shareholders' rights with respect to the remuneration of directors, and transactions with related parties.

2.6 Insufficient involvement of stakeholders (employees)

The greater involvement of all stakeholders, **in particular employees**, in corporate governance is an important factor for ensuring the more long-term approach that must be encouraged and taken into consideration. This includes environmental, social and governance factors, in particular those as referred to in the Principles for Responsible Investment[10] supported by the United Nations.

10 https://pip2022.unpri.org/pip/
The Principles are based on the notion that environmental, social and governance (ESG) issues, such as climate change and human rights, can affect

If, for instance, the majority of shareholders remain passive, do not seek any interaction with the company and do not vote, the **current corporate governance system functions less effectively**. In these circumstances, no corrective action can be expected from the shareholders' side and the supervision of the management rests entirely on the shoulders of the (supervisory) board11.

In measures to improve corporate governance and to assure a more long-term orientation of the administration, **the area of stakeholder participation (e.g., employees) is not considered at all**, despite the great potential held by the structural and financial participation of employees for overcoming unhealthy short-termism and short-sightedness in management.

Employees, for instance, have no influence at all on convocation of the general meeting of shareholders. The convocation rules are very precise in safeguarding shareholders' position; notification of the general meeting must at least indicate precisely when and where the meeting is to take place, and the proposed agenda. Convocation contains a clear and precise description of the procedures shareholders must comply with in order to be able to participate and cast their vote at the general meeting.

Shareholders, acting individually or collectively, have the right to put items on the agenda of the general meeting and table draft resolutions, if each such item is accompanied by a justification. According to company legislation (shareholders' EU Directive 2007/36) and recommendations (the OECD Principles) shareholders have an opportunity to participate effectively and vote at shareholder meetings and be informed of the rules that govern shareholder meetings, including voting procedures. Shareholders are furnished with sufficient and timely information concerning the date, location and agenda of general meetings and regarding the issues to be decided at the meeting. Shareholders are also to be informed about the processes and procedures for shareholder meetings and the principle of

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the performance of investment portfolios and should therefore be considered alongside more traditional financial factors if investors are to properly fulfill their fiduciary duty. The six Principles provide a global framework for mainstream investors to consider these ESG issues. As institutional investors, we have a duty to act in the best long-term interests of beneficiaries. See: Richardson, Benjamin J. (May 21, 2015). Company Law and Sustainability. Cambridge University Press. p. 268. Retrieved June 10, 2020.

11 Action plan 2011.

equitable treatment of all shareholders. **Yet, none of these rights is conferred on the representatives of employees. The representatives of employees are neither invited to the general meeting nor have any rights to speak, ask questions and certainly to cast votes.**

Shareholders have an opportunity to ask questions to the board and propose items on the agenda and resolutions of the shareholder meeting. Shareholders can also ask questions about the external audit report (the OECD Principles). Electing members of the board is a basic shareholder right. Shareholders participate in the nomination of board members and vote on individual nominees, or different lists of them (the OECD Principles). **Employees have absolutely no say or initiative regarding this.**

None of these possibilities is available to employee representatives. Employees have no tools to acquire information at the general meeting, which refers to the company's performance, or to their own position, except for those imposed by some countries in the context of participatory regulation (industrial democracy, co-determination) or those voluntarily conferred by the shareholders.

3. Contemporary EU Corporate Governance Improvements

3.1 Generally on EU and OECD measures to improve corporate governance

A number of EU policy and legal acts since the beginning of the millennium have highlighted the importance of **transparency in the exercise of shareholders' rights** and ensuring their **greater involvement**, which are both keys to better corporate governance.

These acts[12] stipulate that companies need to provide **better information about their corporate governance** to their investors

12 **-EC Communication of 2003 - Modernising Company Law** and enhancing Corporate Governance in the EU - A Plan to Move Forward deals with

and society at large. Investors should be allowed **to know who their shareholders are** and should be more transparent about their voting policies. Shareholders (especially institutional investors, asset managers and proxy advisors) should engage more in corporate governance.

The key corporate governance shortcomings covered by this corporate governance reform were the **insufficient engagement of institutional investors** and **asset managers** and the **inadequate transparency of proxy advisors,** followed by the difficult and costly exercise of investors' rights flowing from securities. In addition, there was an insufficient link between **directors' pay and their performance** and a lack of shareholder oversight on related party transactions.

Long-term shareholder engagement contributes to a considerable improvement in the performance, profitability and efficiency of the respective companies. The long-term commitments of institutional investors (keeping their shares for longer) should provide

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the issue of enhancing shareholders' rights in listed companies and the problems relating to cross border voting.

-**EP Resolution of 2004**, expresses its support for the Commission's intention to strengthen shareholders' rights, in particular through the extension of the rules on transparency in proxy voting, through the possibility of participating in general meetings via electronic means.

-**Agenda 2020 as of 2010** also requires, modern and efficient corporate governance framework for European undertakings, investors and employees; it must be adapted to the needs of today's society and to the changing economic environment.

-**The EP Resolution of 2012** highlighted the importance of corporate governance to society at large, expressing its view on the questions raised by the 2011 Action Plan.

-**Green paper, The EU corporate governance framework,** 2011 COM (2011) 164 final

-**Green Paper on corporate governance in financial institutions** and, stricter rules on corporate governance in financial institutions in the framework of the CRDIV package, 2011.

-**The Shareholders Directive 2007/36**, was based upon this EC Communication EC Green Paper of 2011 on the EU corporate governance framework (Action Plan 2011) outlines the initiatives to modernize the company law and corporate governance framework.

-**The Directive 2017/828, of 17 May 2017, amending Directive 2007/36/ EC** as regards the encouragement of long-term shareholder engagement aims to improve shareholder's engagement, to increase control over directors' remuneration and to restrain transactions with related parties.

more long-term capital to companies. Shareholders' engagement should become more like that of an **'active' owner.**

The EC has made several proposals in the financial sector[13], many of which have now been adopted, to improve corporate governance; for instance, regarding the functioning of boards, risk management, and the remuneration of risk-takers in financial institutions[14].

Pursuant to the **OECD Principles**, the corporate governance framework should provide sound **incentives throughout the investment chain** (long and complex, with numerous intermediaries standing between the ultimate beneficiary and the company) and assure that stock markets function in a way that contributes to good corporate governance.The presence of **intermediaries acting as independent decision-makers** has grown significantly, and many of their assets are managed by specialised asset managers, in turn influencing the incentives and the ability to engage in corporate governance.

Shares of equity investments can be held by institutional investors like **mutual funds, pension funds, insurance companies, and hedge funds.** Still, the ability and interest of institutional investors and asset managers to engage in corporate governance varies widely.

The OECD Principles recommend that **institutional investors disclose their policies** with respect to corporate governance, have direct contact and dialogue with the board and management, and represent other forms of shareholder engagement in frequent use.

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13 Regulation of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012 and Directive of 26 June 2013, on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC (referred as Capital Requirements Directive) In December 2010, the Basel Committee issued detailed rules of new global regulatory standards on bank capital adequacy and liquidity that collectively are referred to as Basel III. The Basel Committee on Banking Supervision (BCBS) has the task of developing international minimum standards on bank capital adequacy.
Following the financial crisis, the Basel Committee has reviewed its capital adequacy standards. Basel III is the outcome of that review.

14 2010 Green Paper on corporate governance in financial institutions (IP/10/656 and MEMO/10/229, 2011 Green Paper on the EU corporate governance framework (IP/11/404), 2013 Green Paper on the long-term financing of the EU economy (IP/13/274).

3.2 The revised Shareholder Rights Directive 2017

The revised Shareholder Directive (EU) 2017/828[15] tackles corporate governance shortcomings related to listed companies and their boards and shareholders (institutional investors, asset managers, intermediaries and proxy advisors) [16]. The revised Directive makes it easier for **shareholders to use their existing rights over companies** and enhance those rights where necessary. This helps to ensure that shareholders **engage more and better hold the company management to account** and act in the long-term interests of the company. It includes **stronger transparency requirements** for institutional investors and asset managers in their investment and engagement policies regarding the companies in which they invest, as well as a framework **to identify shareholders**, to allow them to more easily exercise their (e.g., voting) rights.

The more extensive involvement of shareholders in corporate governance helps to improve companies' performance. This includes environmental, social and governance factors, particularly those referred to in the Principles for Responsible Investment supported by the United Nations.

The aim of revised Directive **2017/828** is to facilitate **interaction between companies and shareholders,** a more long-term focus in corporate governance, and the stronger **involvement of shareholders in corporate governance** as a way to improve the performance of companies.

As concerns long-term shareholder engagement, Directive 2017/828 sets out obligations on intermediaries such as **institutional investors** (undertakings carrying out activities of life assurance and of reinsurance, mutual funds, pension funds, hedge funds)**, asset managers** (investment firms that provide portfolio management services to investors, alternative investment funds) or **management companies, investment companies** and **proxy advisors** (legal persons that on a professional and commercial basis

15 Directive (EU) 2017/828 of 17 May 2017 amending Directive 2007/36/EC (also The directive 2017/828 on long-term shareholder engagement).

16 Main shortcomings in the eye of this Directive 2017/828 are: short-termism, insufficient oversight on directors' pay and related party transactions in interaction between companies and shareholders not effective in cross border situations.

analyse the corporate disclosure and, where relevant, other information of listed companies with a view to informing investors' voting decisions by providing research, advice or voting recommendations related to the exercise of voting rights).

Although the bigger involvement **of all stakeholders**, in particular **employees**, in corporate governance is an important factor for ensuring that a more long-term approach is taken by listed companies, the Directive does not deal with this.

3.3 The right of companies to identify their shareholders

Directive (EU) 2017/828 points out that when shareholders nominate an intermediary, the intermediary should exercise shareholders' rights upon the **explicit authorisation and instruction of the shareholders** and for their benefit; shareholders should know whether their votes were correctly taken into account and should have the possibility **to verify after the general meeting** whether the vote was validly recorded and counted by the company.

Confirmation of the receipt of votes should, according to Directive (EU) 2017/828, be provided in the case of electronic voting. Directive 2017/828 establishes a high level of **transparency with regard to charges,** including prices and fees, for the services provided by intermediaries. Discrimination between charges for the exercise of shareholder rights domestically and on a cross-border basis is prohibited.

Directive (EU) 2017/828 gives **companies the right to identify their shareholders** (Article 3a). Listed companies hence have the right to identify their shareholders in order to be able to communicate with them directly. Intermediaries are required upon the request of the company to communicate to the company the information regarding the identity of a shareholder. However, member states should be allowed to exclude from the identification requirement shareholders that only hold a small number of shares (no more than 0.5% of shares).

The following information on shareholder identity, as set out by Directive (EU) 2017/828, must be transmitted to the company (any less information would be insufficient to allow the company to identify its shareholders in order to communicate with them): the name and contact details of the shareholder and the registration number or, a unique identifier (where the shareholder is a legal person), the number of shares the shareholder holds and the categories or classes of shares held and the date of their acquisition. Less information than stated by Directive 2017/828 would be insufficient to allow a company to identify its shareholders in order to communicate with them.

The company and the intermediaries are **allowed to store personal data relating to the shareholders** for as long as they remain shareholders. Yet, companies and intermediaries are often unaware that a person has ceased to be a shareholder unless they have been informed by the person, or have obtained that information through a new shareholder identification (that takes place only in relation to the annual general meeting or takeover bids or mergers). Companies and intermediaries should thus be allowed to store personal data until the date on which they become aware that a person has ceased to be a shareholder and for a maximum period of 12 months after that date (Directive (EU) 2017/828).

To summarise, companies have **the right to collect and store personal data of their shareholders** in order to **identify their existing shareholders** to communicate with them directly, with a view to facilitating the exercise of shareholder rights and shareholder engagement with the company (for as long as they remain shareholders).

3.4 Shareholders exercising their rights through intermediaries

When shareholders nominate an intermediary (Directive (EU) 2017/828), the intermediary should exercise the shareholders' rights **upon the explicit authorisation and instruction** of the shareholders and for their benefit. Shareholders should know **whether their votes were correctly taken** into account and should have the possibility to verify after the general meeting whether **the vote was validly recorded** and counted by the company.

Confirmation of the receipt of votes should be provided in the case of electronic voting under Directive 2017/828. The chain of intermediaries may include 'third-country' intermediaries. These are intermediaries that have neither their registered office nor their head office in the EU. Nevertheless, the activities carried out by third-country intermediaries may have effects for the long-term sustainability of EU companies and corporate governance in the EU. Third-country intermediaries are therefore subject to the rules on: shareholder identification, transmission of information, facilitation of shareholder rights, and transparency and non-discrimination of costs.

It is necessary to ensure that **information is transmitted throughout the chain** of intermediaries. Directive 2017/828 establishes a high level of **transparency with respect to charges**, including prices and fees, for the services provided by intermediaries. Discrimination between the charges for the exercise of shareholder rights domestically and on a cross-border basis is prohibited. Any differences between what is charged for the domestic and the cross-border exercise of shareholder rights should only be allowed if they are properly justified and reflect the variation in intermediaries' actual costs incurred for delivering the services.

3.5 Institutional investors, asset managers, proxy advisors

Institutional investors and asset managers are important shareholders of listed companies in the EU. However, institutional investors and asset managers **do not engage with the companies** in which they hold shares. This means they could jeopardise the long-term financial and non-financial performance of companies, often being non-transparent about their investment strategies and their engagement policy and implementation thereof. Institutional investors and asset managers are often not transparent when it comes to their investment strategies, engagement policy and related implementation.

Directive (EU) 2017/828 hence requires institutional investors and asset managers **to be more transparent** in shareholder engagement. It requires that the policy on shareholder engagement (which should be publicly available online) include:

– how institutional investors and asset **managers integrate shareholder engagement into their investment strategy;** and
– how to **manage actual or potential conflicts of interest** (situations in which institutional investors or asset managers have significant business relationships with the investee company).

To summarise, the new Article 3h provides that member states must ensure that institutional investors publicly disclose how the **main elements of their equity investment strategy** are consistent with the profile and duration of their (particularly long-term) liabilities and how they **contribute to the medium- to long-term** performance of their assets.

Asset managers should according to Directive (EU) 2017/828 give information to the institutional investor that is sufficient to assess whether and how the manager is acting in their **best long-term interests** and pursuing a strategy that provides for efficient shareholder engagement. If the assets are managed on the basis of a discretionary mandate, for smaller and less sophisticated institutional investors it is crucial to establish a minimum set of legal requirements so that they can properly assess the asset manager and hold them to account.

As stipulated in Directive (EU) 2017/828, **asset managers** should be required to **disclose to institutional investors:**

– how their investment strategy and pertaining implementation contribute to the **medium- to long-term performance** of the institutional investor's assets; and
– the key material **medium- to long-term risks** associated with the portfolio investments, including corporate governance matters and other medium- to long-term risks, allowing the institutional investor to assess whether the asset manager is carrying out the medium- to long-term analysis of the equity and the portfolio, which is a key enabler of efficient shareholder engagement.

Proxy advisors are companies specialised in analysing company disclosures and providing advice to investors concerning how they should vote at the general meeting of shareholders. Proxy advisors provide research, advice and recommendations on how to vote at general meetings; they play an important role in corporate governance, and contribute to reducing the costs of the analysis of company information.

Proxy advisors may also have an important influence on the voting behaviour of investors (especially investors with highly diversified portfolios and the many foreign shareholdings that rely more on proxy recommendations).

Legislation generally accepts that voting by proxy is permitted. Every shareholder has the right to appoint any other natural or legal person as a proxy holder to attend and vote at a general meeting in their name. The proxy holder enjoys the same rights to speak and ask questions at the general meeting. **Although proxies should vote according to the direction of the proxy holder, in reality this does not always happen**. This is the reason for the important changes related to proxy disclosure that we describe in a separate chapter. The OECD Principles, even before these changes, recommended that the directions for voting should be disclosed where proxies are held by the board or the management for company pension funds and for ESOP.

Under Directive (EU) 2017/828, proxy advisors are subject to a code of conduct on **transparency requirements** and **must report their application** of that code. Proxy advisors should also **disclose:**

– key information on research, advice and voting recommendations; and
– any actual or potential conflicts of interest or business relationships that could influence the preparation of the research, advice and voting recommendations. That information should remain publicly available for a period of at least 3 years.

4. Conclusion

Ownership concentration leads to **shareholders activism**, which causes **short-termism** in the maximisation of profits, as one of the serious reasons for inefficient and poor business performance. The company law concept (the legislative framework for directors' duties and liabilities) does not provide a basis for shareholder activism; however, it does not prevent it successfully. Shareholders' activism and **managerial short-sightedness** (myopia) as the process of decision-making in concentrated ownership companies is not even explicitly legally prohibited.

The EU's measures, like the right of companies to identify shareholders, regarding more transparency and disclosure in exercising shareholders' rights through intermediaries and the stricter obligations of institutional investors, asset managers, proxy advisors, will definitely contribute to more transparency and responsibility in corporate management. **Yet, the question is whether these measures will eliminate the short-termism and short-sightedness** of corporate and managerial decisions which is becoming such a widespread practice that the theory views it as a systemic error.

This is especially because the measures for more long-term corporate governance do not include any greater **consideration of the interests of employees** and other **stakeholders**, who by far care the most about the company's long-term success.

While **several measures have been imposed in the EU** to try to **overcome these shortcomings**, no measure in either the EU measures nor those of the OECD involve those who hold the greatest interest in the corporation's long-term success because their existence depends on it, i.e., the **employees**. The ideological barriers are too great. Disregard of the structural measures needed to strengthen the position of employees whose long-term stability is of the highest natural interest is an enormous shortcoming of all the anti-short-termism measures and has its origins in the ideological systemic exclusion of employees from decision-making.

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DAMAGE AND CRIMINAL LIABILITY OF THE MANAGEMENT AND SUPERVISORY BOARD MEMBERS OF COMPANIES FROM PRIVATE AND PUBLIC SECTOR BOTH WITHIN AND OUTSIDE THE GROUP OF COMPANIES

Borut Bratina, Peter Podgorelec

Abstract

This article systematically shows the duties of the management and supervisory board members and analyses the current development of their liability on both legislative and case law level. On the legislative level, a problem exists in form of the ten-year limitation period. Another problem is the legal protection of shareholders/company members of subsidiaries in cases when the majority holdings are not held by a company but by a different legal subject, by a state or a municipality, for example. In this respect, suitable solutions are proposed. Criminal offence of abuse of position or trust in business activity requires existence of a serious and evident infringement that causes significant damage. Authors criticise the existing case law as regards the rulings on the said criminal offence in connection with one-person limited liability companies. In the article, comparative and normative-dogmatic methods are used predominantly.

Key words: companies – board members – damage liability – criminal liability – business judgment rule – interest of the company – group of companies

1. Introduction

Delegated management under the board structure is one of the basic legal characteristics of companies. Shareholders do not run the business themselves (as in partnerships), but leave the running of business (along with the supervision thereof) to specific bodies of the company (management and supervisory bodies). Third parties can also be members of those bodies, however, this gives rise to the problem of assuring that these third parties (»hired directors«) follow the interests of capital owners and give those interests advantage over their own. One of the ways to resolve this problem is to set the rules and standards that have to be followed by the members of management and supervisory bodies. Rules strictly define how the directors must act and, equally, how they must not, while standards typically leave the precise determination of compliance to the courts »after the fact«. Legal restrictions, in the form of rules or standards, are of course of no meaning if their infringement is not suitably sanctioned, mostly in the form of damage liability and, in extreme cases, criminal liability. Both types of (legal) liability are the subject of this article which aims at systematically displaying the duties of management and supervisory board members and critically analysing the newest development of those duties, including the sanctioning of their violations on both legislative and case law level. The differences between private and public sector companies[1] are mostly apparent in case of integration of companies into groups. In that respect a question arises as to whether the minority shareholders and creditors of subsidiaries enjoy suitable legal protection when it comes to the interweaving of private and public interests. On the other hand, the dilemma that exists in the area of criminal liability is how to interpret the element of unlawfulness in the scope of the criminal offence of abuse of position or trust in business activity which is one of the most frequent reasons for criminal prosecution of managers.

2. Damage Liability

If the members of management or supervisory bodies violate their duties – the latter can be divided into the duty of care and the duty of loyalty – they are liable towards the company for the damage caused. Both abovementioned duties stem from Article 263 of the Slovenian Companies Act (ZGD-1) which presents a general clause on liability of members of management and supervisory bodies and is applicable to both private and public sector companies. The first paragraph of the said article stipulates that members of a management or supervisory body shall act for the good of the company with the diligence of a conscientious and fair manager and safeguard the trade secrets of the company. Because there is no need to provide evidence showing that the duties were violated intentionally, damage liability is significantly easier to prove than criminal liability. Accordingly, it presents an easier way for the company to compensate the incurred losses, especially in case the company

1 The term »public sector« is not uniformly defined. In this article, the definition from the Integrity and Prevention of Corruption Act (ZIntPK) is used.

has D&O insurance in place. However, it needs to be immediately pointed out that a business decision which turns out to be wrong does not necessarily present a violation of the duty of acting diligently. When assessing liability – not only liability for damages, but also criminal liability – business judgment rule needs to be considered. Even though it is not enacted in the form of a legal norm in Slovenian legislation, it has been adopted and enforced by case law (see section 3).

2.1 Duty of care

Duty of care stipulated in the first paragraph of Article 263 of ZGD-1 has two functions: on one hand it acts as a benchmark for assessing guilt, while on the other hand it presents a general clause that is the source from which case law and legal theory derive specific duties of conduct in case they are not specifically prescribed by law, articles of association or the contract on performance of the function (Hüffer and Koch, 2018: 624). When assessing whether certain conduct meets the standards of conscientious and fair management, the assessment shall be done exclusively on the basis of objective criteria (abstract criteria of assessment). As correctly pointed out by the German Federal Court of Justice in case No. II ZR 143/93 of 20 February 1995, members of the management board are trustees of foreign property which was entrusted to them for the purpose of management and increasing of its value. This requires a higher degree of their diligence. In its decision in case No. III Ips 75/2008 of 21 December 2010, Supreme Court of the Republic of Slovenia took a correct position that members of the management board (and also of supervisory bodies – note by the authors) are required to act with stricter, professional diligence. Duty of care provided for in the first paragraph of Article 263 of ZGD-1 thus correlates with the duty of care from the second paragraph of Article 6 of the Slovenian Code of Obligations (OZ). The latter stipulates that, in fulfilling obligations proceeding from their professional activities, participants in obligational relationships must act with greater diligence, according to the rules and custom of the profession (the diligence of a good expert).

Supervisory board does not supervise all of the company's business, but only the more important operations. Matters on which the management board needs to report to the supervisory board in accordance with the first paragraph of Article 272 of ZGD-1 can be used for orientation. Criteria to be followed by the supervisory board in exercising supervision are legality, correctness and economy of supervised business activities (Lutter and Krieger, 2008: 58 – 63). Assuring the legality of business is one of the management board's fundamental duties, which makes it crystal clear that the supervisory board needs to pay special attention to how the management board complies with this duty. Of course, the supervisory body is not liable for every infringement that occurs in the company, however, if it learns, in any way, of a suspicion that an infringement has occurred, especially on the management board level, it needs to take immediate action. In Slovenia, through amendment ZGD-1I, position of the internal auditor has been strengthened and the possibility of direct cooperation between the internal auditor and the supervisory board has been introduced (Article 281.a of ZGD-1). Such direct cooperation is expected to reinforce the independence of the internal auditor and thereby to increase the efficiency of the supervisory board (Podgorelec and Kolar, 2020: 222 – 223).

It is typical for the two-tier governance system that the management and supervisory functions are strictly divided and split into two different bodies, the management board and the supervisory board. However, a public limited company can opt also for one-tier governance system where the two functions are united within one and the same body, the board of directors. The board of directors can name one or more executive directors, however, it can only delegate to them the responsibility of day-to-day management and some other tasks prescribed by law, while it remains responsible for running the company and for the supervision of executive directors' actions. In the one-tier system, duties of diligent conduct are thus intertwining within a single body (the board of directors), while they are divided between two separate bodies in the two-tier system. Executive directors are, in formal sense, not a body of the company, however, they are operators of corporate tasks prescribed by law, by articles of association or by rules of procedure, and are subject to Article 263 of ZGD-1 which governs the diligence and liability of members of management and supervisory bodies. Consequently, executive directors can be defined as a company body in material sense (Podgorelec, 2010: 428).

2.2 Duty of loyalty

Duty of loyalty means that the members of management and supervisory bodies need to be loyal to the company and must always act in line with the company's interests. The duty of loyalty has two dimensions that are partially overlapping. The first dimension is the prohibition of obtaining special benefits: members of the management board, supervisory board, board of directors and executive directors must not exploit their function for obtaining personal benefits or benefits for third parties whose interests may be in conflict with the interests of the company. Typical cases are exploitation of company's business opportunities, bribery and insider trading. The second dimension relates to the prevention and control of conflicts of interests in which the members of management and supervisory bodies may find themselves. As a basic rule, in such conflicts the interests of the company – in all regards – prevail over personal interests. On this subject, ZGD-1 includes the provisions on the transfer of representation authorizations to the president of the supervisory board in case of a transaction between the company and the member of the management board (Article 283 of ZGD-1), on the approval of a loan (Article 261 of ZGD-1) and on the non-compete obligations (Article 41 of ZGD-1). Regulation of business with members of management and supervisory bodies and with the persons related to them, such as with their family members and with the companies in which they can exercise a dominating influence, is part of o broader related-party transactions concept, introduced into Slovenian legislation through amendment ZGD-1K (2021) (Podgorelec, 2021: 66).

2.3 Amendment ZGD-1I

Article 263 of ZGD-1 was last amended with the adoption of amendment ZGD-1I in 2015. Modifications which need to be pointed out the most are the ones relating to the conclusion of D&O insurances and to the length of limitation periods. According to the new amendment, conclusion of D&O insurance remains voluntary, however, if the company concludes such insurance to the benefit of its »managers« and possibly also its officers, a deductible needs to be agreed upon in a value specifically prescribed by law. This amendment can be rated as positive, since the obligatory deductible maintains the preventive function of damage liability. Yet, the new regulation of limitation periods cannot be evaluated positively, since the amendment ZGD-1I privileges the companies in which the state or a municipality have a dominating influence. Namely, these companies can assert their damage claims within ten years as from the occurrence of damage, while all other companies are bound by a five-year limitation period. There are no legitimate reasons for such differentiation, which is why legal theory (Kocbek, 2015: 1072) drew attention to the unconstitutionality of such regime shortly after the adoption of the amendment. The fact that the state or a municipality have a dominating influence in a company does of course not mean that the detection of suspected infringements of management and supervisory bodies' members' duties and the determination of incurred damage are in any manner more difficult than in all other companies. The provision on the ten-year limitation period is a highly »political provision« that should be abolished as soon as possible.

3. Business Judgment Rule

Business judgment rule is a rule used for assessing liability as regards business decisions. These decisions are not legally regulated and their actual consequences are, in most cases, not fully foreseeable. Consciously taking risks, which is typical for business activity, is always connected with the threat of misjudgements and wrong assessments. Every manager is exposed to this danger, regardless of his best endeavours to act diligently. To enable managers to take reasonable risks, which is not only in the best interest of the company and its shareholders as the company's beneficial owners but also in the interest of national economy, without constant fear of possible lawsuits, business judgment rule was established, first in the United States and later also in other parts of the world. In most cases, the rule has been established in case law, while some countries, including Germany, Austria and Croatia, have enacted business judgment rule in their legislation. In Slovenia, there has also been an attempt to enact the business judgment rule within amendment ZGD-1I, however, the line ministry abandoned such an intention during the inter-ministerial coordination. Consequently, the establishment of the rule remains fully in the hands of case law. In this regard, decisions of the Slovenian Supreme Court No. III Ips 75/2008 of 21 December 2010, No. III Ips 80/2010 of 9 July 2013 and No. III Ips 97/2015 of 9 December 2015 are of special relevance (Podgorelec, 2017: 718), since they indicate that Slovenian case law recognizes business judgment rule and specifically takes it into account when interpreting required diligence of members of management and supervisory bodies. Business judgment rule means that a member of a management or a supervisory body is not liable even if a certain operation resulted in a loss for company, as long as prescribed preconditions have been met. These preconditions are: business nature of the decision, adequate base of information, decision-maker's good faith and acting exclusively in company's interest. Crucial is the *ex-ante* aspect of assessment. Said differently: conduct of a member of a management or a supervisory body meets the required standard of professional diligence if the member in question could have reasonably assumed that he acted on the basis of adequate information and in the company's interest. Even though damage has been caused to the company, damage liability of the member of management or supervisory body is in such case excluded in accordance with the second paragraph of Article 263 of ZGD-1, since the element of unlawfulness is missing. The same should be applicable also when assessing criminal liability under Article 240 of the Slovenian Criminal Code (KZ-1). A failed business decision should not lead to criminal liability for committing an offence of abuse of position or trust in business activity. Such a decision can only become relevant in terms of both, civil and criminal law, if the boundaries of safe harbour provided by business judgment rule have been breached, and, of course, if other preconditions for criminal liability have been met. More on this topic in section 6.2 below.

4. Interest of the Company

ZGD-1 does not define what determines the interest of the company: is it only the interest of shareholders (the so-called shareholder-value concept), or should it be interpreted broader, taking into account also interests of other groups that are in some way linked to the company, especially interests of workers, creditors and of community at large (the so-called stakeholder-value concept). The differences between the two concepts are not significant, since, lately, advocates of the shareholder-value concept concentrate only on the long-term shareholders' interest, aimed at a sustainable growth of the company, which indirectly considers also the interests of other stakeholders (Hüffer and Koch, 2018: 467). The pure shareholder-value concept where the interest of the company is determined exclusively by maximisation of the equity capital's value is increasingly being abandoned. A good example are the developments in Great Britain where the so-called enlightened shareholder-value model has been enacted in the Companies Act (CA – 2006 – Article 172). This model requires the managers to consider, in the context of promoting the benefit of the members and shareholders, also the interests of other stakeholders (Mayson, French and Ryan, 2008: 469), for example of workers, suppliers and consumers. Additionally, special emphasis is given to the necessity of the assessment of company's influence on society and environment and to the requirement of taking into consideration probable long-term consequences of the company's actions. Such concept of company's interests corresponds also to Slovenian corporate law (Podgorelec, 2014: 711 – 713). Accordingly, when making business decisions, members of management and supervisory bodies need to consider the effect of those decisions on the long-term and sustainable development of the company. Even though a certain business decision has a direct economically adverse effect, it remains allowed if it can be reasonably expected that the decision will result in long-term benefits for the company. On the other hand, business decisions with immediate economic benefits but with long-term negative effects on society are deemed problematic (Walden, 2020: 52).

5. Group of Companies

Slovenia is one of those countries that have relationships between linked companies specifically regulated within their corporate legislation – the law of groups (part IV of ZGD-1, Articles 527 – 562). Even though ZGD-1 governs three different types of groups of companies – a de facto group, a contractual group and an integration, mostly de facto groups have been established in practice. Moreover, grouping of companies into de facto groups is, in fact, the predominant way the economy is organised. There are far less contractual groups and almost no integrations, which is why these two types of groups will no longer be discussed in this article. For de facto groups, it is characteristic that the dominant company and one or more dependent companies are linked under unified direction of the dominant company (item 1 of the first paragraph of Article 530 of ZGD-1). The purpose of special arrangement of de facto groups is to increase legal protection of minority shareholders and creditors of dependent companies. This goal is achieved through the transparency of relations between the company, its dominant owners and other companies linked to such owners. Correspondingly, the dependent company needs to draw up a dependence report (third paragraph of Article 545 of ZGD-1) which includes all legal transaction entered into by the company with the dominant company or its affiliates and all other acts that the company carried out or failed to carry out at the initiative or in the interest of these companies. The report needs to be reviewed by the auditor that audits the annual report (Article 546 of ZGD-1). Supervisory board of the dependent company has special obligations too and needs to review the dependence report, while it also needs to draw up its own report (Article 546.a of ZGD-1). Since the amendment ZGD-1I, a special audit of business relations between the company and the dominant company or its affiliates is foreseen (Article 546.b of ZGD-1) and can be proposed to the court by any company's shareholder/member. For any uncompensated losses, damage liability lies not only with the dominant company, but also with its representatives who executed the adverse influence (first and second paragraph of Article 547 of ZGD-1). Claim for damages may be pursued by any shareholder, not only by the minority of shareholders as in accordance with general rules (third paragraph of Article 547 of ZGD-1 in connection with the fourth paragraph of Article 543 of ZGD-1). Such regime is based on the premise that there is an increased threat with certain holders of shares, predicting that they may exercise their possibility of dominant influence contrary to the interests of the company, thereby harming the company, its minority shareholders and creditors. These are those shareholders/members who pursue the economic interests also outside the company by having controlling shares in other companies or who are directly carrying out economic activities themselves.

A problem arises when the holder of the majority share is not a company but a different legal subject, for example the state or a municipality, since such positions are – at least according to grammatical interpretation – not covered by the abovementioned safeguarding provisions (Podgorelec and Bratina, 2014: 127 – 143). In such cases, problematic is not only the threat of conflicts of economic interests that the holder of the majority share pursues in different companies, but also the threat of conflicts between economic and political interests. A conflict between politics and economy is in no aspect less dangerous than a conflict between different economic interests (Raiser, 1996: 465). Accordingly, in such cases the same safeguards shall be applicable as are in the case when the holder of the controlling share is a company.[2] The position of minority shareholders/members and creditors, along with the need of their protection, cannot be dependent on the legal status and characteristics of the subject that is able to exercise its controlling influence in the company (Juhart, 2007: 14). There are three possible solutions which could eliminate this inconsistency: a) analogical use of law of groups (Rozman, 2016: 90 – 92); b) a specific provision in ZGD-1 indicating which legal subjects that can exercise controlling influence are equal to the controlling company; c) transition to the German solution where the definition of a controlling shareholder/member is conceptually open and left to teleological interpretation (Podgorelec, 2016: 1020). In Germany, there are no dilemmas whether the state or municipalities can be treated as »controlling companies« and are therefore fully subject to the rules of the law of groups (Emmerich and Habersack, 2005; 28 – 30; Drygala, Staake and Szalai, 2012: 631).

2 It is true that there are special regimes that govern the corporate-law position of certain legal subjects as owners of capital shares. Such a case is, for example, management of state's corporate investments. However, the recently adopted Slovenian Sovereign Holding Act (ZSDH-1) does not lead to a different conclusion. Procedures and criteria that should limit political influence on the choice of candidates for members of supervisory bodies, along with the exclusion of possibility to give management bodies mandatory instructions, are not a sufficient warranty that there will be no influence on business decisions.

6. Criminal Liability

Duty of care of management and supervisory body members who manage foreign assets is governed by the first paragraph of Article 263 of ZGD-1. Breach of this duty can lead to damage liability towards the company and, as *ultima ratio*, also to criminal liability of members of management and supervisory bodies. However, it needs to be addressed how and using which criteria can one differ between business conduct that is undoubtedly criminal and conduct that cannot be defined as such, while the consequence of both is company's bankruptcy as a general term for various manifestations of economic failure (Bacon, 2017: 165). The doyen of Slovenian criminal law, prof. dr. Ljubo Bavcon, rightly warned about the difficulty of distinguishing between what is only a bad business decision and what a criminal offense and about the fact that criminal repression is not and cannot be a suitable means for resolving social, political and economic problems and conflicts (Bavcon, 2017: 165). Economic crises are an inevitable consequence in a capitalist socio-economic system, especially in its neoliberal version. Society organized in such a way is a highly risky society, there are no actions which surely and foreseeably lead to profits, which is why there are numerous wrong economic-political decisions of the European Commission, the Slovenian government and central or other banks, in addition to missed, wrong, panicked and also incriminated business decisions of certain economic actors (Bavcon, 2017: 166).

First paragraph of Article 1 of the Slovenian Criminal Code (KZ-1) stipulates that criminal liability in the Republic of Slovenia may be imposed while respecting constitutionally provided human rights and fundamental freedoms in a democratic arrangement and on the principles of a state governed by the rule of law. Two basic maxims of the principle of legality in criminal law are the principles *lex praevia* (the law must be known when the criminal offence is committed) and *lex certa* (the law must be clearly defined). The first principle is enacted in Article 2 of KZ-1 which states that no sentence or other criminal sanction can be imposed on any person for committing an offence that did not constitute a criminal offence under the statute prior to being committed, and for which a sentence was not prescribed by the statute. The second principle needs to be followed by both the legislator (when defining particular criminal offences) and the law enforcement authorities and courts when addressing (prosecuting) perpetrators of criminal offences. In Chapter 24, KZ-1 includes a total of 26 criminal offences against the economy. Article 240 of KZ-1 incriminates abuse of position or trust in business activity and has become, in recent years, one of the most commonly used provisions for prosecution of economic crime (Kovačič Mlinar, 2017: 171).

6.1 Criminal offence of abuse of position or trust in business activity

This criminal offence is committed when someone, in the governing or supervising of an economic activity, abuses his position or the trust placed in him for disposing of another's property, managing a company, or conducting a business activity, acts beyond the limits of the rights inherent in his position or fails to perform any of his duties based on law, other regulation or legal transaction, and procures an unlawful property benefit for himself or for a third person or causes damage to the property of another. The said criminal offence was modified in 2017 by amendment KZ-1E. Before the amendment, it was stipulated that this offence is committed when someone, in the governing or supervising of an economic activity, »with a view to procuring an unlawful property benefit for himself or for a third person or to causing damage to the property of another abuses his position or the trust placed in him…« The provision required »coloured« intent (*dolus coloratus*) which, in practice, is very difficult to prove. On the other hand, the basic form of this criminal offence did not require any damage to the property of the company to occur, which – in both, theory and practice – raised the question as to which interest is in fact legally safeguarded in relation to this criminal offence. With an aim of eliminating such doubts and bringing the description of the criminal offence closer to the same criminal offence in other neighbouring countries (for example to the arrangements in Germany and Austria – *»Untreue«*), amendment KZ-1E modified the description and implemented the version that is in force today. Nevertheless, certain dilemmas still remain and will be discussed below.

6.2 Criminal offence of abuse of position or trust in a one-person limited liability company

There have been situations in Slovenian case law where the only company member who was simultaneously the manager of »his own company« has been accused and later convicted of a criminal offence of abuse of position or trust in business activity (e.g. decision of the Higher Court of Ljubljana, No. II Kp 15577/2011 of 4 July 2017). A more in-depth corporate law analysis shows a completely failed application of the criminal offence of abuse of position or trust in regard to one-person companies, since it is conceptually impossible to »abuse the trust towards yourself«[3] and, similarly, to cause damage to yourself (economic owners are shareholders). As for limited liability companies, ZGD-1 stipulates that a claim for damages against the managers can only be filed with the consent of company members who have an option to select a special representative for filing the damages claim against (the former or current) manager. In case of a one-person limited liability company where the only company member is also its manager, this only member is the one that should give his consent to file a claim for damages against himself. For such cases, ZGD-1 does not envisage a special representative that would be named by the court and would represent the company against the only company member. Corporate legislation (ZGD-1) does not foresee compensation claims in such cases. Accordingly, prosecution of the criminal offence of abuse of position of trust is, in such cases, completely unnecessary and unsystematic. However, it still is possible that the only company member as the manager of a one-person limited liability company commits some other criminal offence against the creditors, buyers, consumers or the state (tax evasion or smuggling).

3 A company is a legal person (first paragraph of Article 3 of ZGD-1) and as such an independent legal subject, however, there is no »trust relationship« between the director and the company but only between the director and company members.

6.3 Free economic initiative and criminal law

Constitution of the Republic of Slovenia stipulates in Article 74 that free economic initiative shall be guaranteed and that the conditions for establishing commercial organisations shall be established by law. Furthermore, it also stipulates that commercial activities may not be pursued in a manner contrary to the public interest and that unfair competition practices and practices which restrict competition in a manner contrary to the law are prohibited. Accordingly, the basic question is where the free economic initiative ends and where the legitimate interest of the state in form of criminal repression begins (Kovačič Mlinar, 2017: 171). Slovenian Constitutional Court has also addressed these questions and has adopted a clear position that restricting the free economic initiative by legislation is allowed only if such restrictions are urgent in order to protect a more important public good (for example: protection of health, of consumers and creditors, etc.), provided that the restrictions also meet the conditions of appropriateness, proportionality and limited durability, are clear and do not interfere with the equality of the subjects (Kovačič Mlinar, 2017: 172). The said conditions need to be considered already by the legislator when incriminating particular offences against the economy. The criminal offence of abuse of position or trust in business activity was initially conceived as a subsidiary criminal offence and the state prosecutor first needed to determine whether the actions possibly contained the elements of some other criminal offence (Ferlinc, 2016: 6). Through practice, the mentioned criminal offence became the most used independent criminal offence. Because this criminal offence is governed by a so-called (quiet) blanket norm, the elements of unlawful conduct need to be searched for in the corporate legislation, which puts a question mark to the compliance with the constitutional and legal principle *lex certa* (Kovačič Mlinar, 2017: 177).

Some authors (Bavcon, 2017: 167) rightly warn that the principle of due (professional) diligence is intended for use in determining civil damage liability and that uncritical use of the said principle within criminal law can be disputable from the viewpoint of *lex certa*. On the other hand, the Slovenian Constitutional Court and also the Slovenian Supreme Court have adopted a clear position that, as regards the criminal offence in question, determination of the elements of the criminal offence depends on ZGD-1, meaning that the provisions of ZGD-1 need to be considered when determining the existence of the criminal offence of abuse of position or trust in business activity (decision of the Constitutional Court of the Republic of Slovenia, No. U-I-268/05 of 5 July 2007, decisions of the Supreme Court of the Republic of Slovenia, No. I Ips 35999/2015-165, No. I Ips 7935/209-44 and No. I Ips 134/2009). In each particular case, the court needs to answer the question as to whether the person abused its position when performing business activity, taking into account the rules and regulations of corporate law which govern the field of the person's assumed criminal activity. Moreover, this means that criminal courts shall, when assessing the diligence under Article 240 of KZ-1, also use, without exception, the business judgment rule that was clearly adopted by Slovenian case law (Podgorelec, 2013: 763). When applying the duty of care governed by the first paragraph of Article 263 of ZGD-1, it needs to be considered that the absence of damage liability of the members of management or supervisory bodies also means that there is no unlawfulness in terms of criminal liability. Rules of corporate law need to be considered comprehensively, meaning that due professional diligence needs to be assessed by taking into consideration also the autonomous rules of corporate law, such as good business customs, corporate governance code, ethical codes of various associations of businessmen (for example: Managers' Association of Slovenia, Slovenian Directors' Association), rules of the financial profession, etc.

When analysing the influence of corporate law on the assessment of liability for the criminal offence under Article 240 of KZ-1, it is sensible also to look into certain decisions of German courts. Namely, it was exactly the German arrangement of the *Untreue* criminal offence under Article 266 of the German Criminal Code which presented a model for the Slovenian legislator when including the criminal offence of »abuse of position or trust« (and its predecessors) into Slovenian criminal legislation. The German Federal Constitutional Court clearly warned (in its decision No. 2 BvR 2559/08 of 23 June 2010) of an extremely broad room of manoeuvre given to the members of management and supervisory bodies who can – and sometimes even must – take certain risky decisions. Accordingly, the fact that a decision sometimes »does not bear fruit« is not sufficient to define such a decision as unallowed or even illegal. Regarding due diligence, the German Federal Court of Justice (decision No.

1 StR 185/01 of 15 November 2011) pointed out that no violation of due diligence can be claimed only because a risk connected to a certain business decision actually came true. Additionally, the court noted that ex-post assessment of conduct is not allowed. In accordance with German case law, it is not every non-diligence that suffices for establishment of unlawfulness in terms of criminal liability, but only material breaches of due diligence (Regional Court of Hamburg, decision No. 608 KLs 12/11 of 9 July 2014). The highest German courts (Federal Constitutional Court and Federal Court of Justice) have, through years of deciding on incriminated actions of members of management and supervisory bodies, established clear positions on which violations of due professional diligence are relevant in terms of criminal liability. It follows from German case law as well as from German legal theory that the violation of due diligence is material and relevant for establishment of the *Untreue* criminal offence if the violation is evident (does not need a more precise assessment of conduct) and »plain as day« (is crystal clear also to a layperson), and if the decision is completely unreasonable or outside the regular scope of company's business. (Wagner, 2019: 360).

7. Conclusion

Decisions made by members of management and supervisory bodies can be divided into two groups – legally bound and legally unbound decisions, the latter being more frequent. For those decisions, it is typical that the decision-maker can choose between different alternatives, which also includes the option to take no measure at all. Liability for legally unbound decisions is assessed in accordance with the business judgment rule which is not formally enacted in Slovenian legislation, however, it was clearly established by Slovenian case law. Such development in determination of damage liability is in line with the developments in comparable legislations, with German legislation as one of the examples. Interest of the company is not short-term maximisation of equity capital's value, but a long-term and sustainable growth of the company. Even though a certain business decision has a direct economically adverse effect, it remains allowed if it can be reasonably expected that it will result in long-term benefits for the company.

In 2015, amendment ZGD-1I introduced two important novelties. The first novelty relates to the D&O insurance, while the other one affects the length of limitation periods. According to the new arrangement, conclusion of D&O insurance remains voluntary, however, if the company concludes such insurance, a deductible needs to be agreed upon in a value specifically prescribed by law. This amendment can be seen as positive, since the obligatory deductible maintains the preventive function of damage liability. On the other hand, the same cannot be said for the newly stipulated limitation periods. Namely, amendment ZGD-1 has put the companies in which the state or municipality have a dominating influence in a privileged position. These companies can assert their damage claims within ten years as from the occurrence of damage, while all other companies are bound by a five-year limitation period. There are no legitimate grounds for such differentiation. The provision on the ten-year limitation period is a highly »political provision« that should be abolished as soon as possible.

In Slovenia, relationships between linked companies are specifically regulated by corporate legislation – the law of groups (part IV of ZGD-1, Articles 527 – 562). The purpose of special arrangement is to increase legal protection of minority shareholders and creditors of dependent companies. A problem arises when the holder of the majority share is not a company but a different legal subject, for example the state or a municipality, since such positions are – at least according to grammatical interpretation – not covered by the law of groups. There are three possible solutions which could eliminate this inconsistency: a) analogical use of law of groups; b) a specific provision in ZGD-1 indicating which legal subjects that can exercise controlling influence are equal to the controlling company; c) transition to the German solution where the definition of controlling shareholder/member is conceptually open and left to teleological interpretation by the courts and legal theory.

In Slovenian case law and legal theory, it should be clearly defined when the violation of duty of care presents an infringement which gives rise also to criminal liability for the offence of abuse of position or trust under Article 240 of KZ-1. The violation should certainly be grave and evident, while it should also cause greater damage. For minor violations and smaller damage, ZGD-1, within its penal provisions, prescribes a number of minor offences that can be committed also through negligence and for which the fines may be imposed on members of management and supervisory bodies, other persons in charge and on companies as such. In case of one-person limited liability companies, the current criminal case law is completely wrong, since it is not possible to »abuse the trust towards yourself« or to cause damage to yourself.

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A NEW CHALLENGE IN CORPORATE GOVERNANCE – THE NEW LEGAL REGULATION OF NON-FINANCIAL REPORTING

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Abstract

The effectiveness of corporate governance has no longer been judged solely based on short-term financial returns. Shareholders and the broader social community increasingly demand long-term value creation and non-financial performance. Corporate social responsibility has become a global phenomenon, addressed by academics and by major international organisations, including the OECD and the EU. Directive 2014/95/EU introduced the obligation to report certain non-financial information for large public interest corporations, making it the first legal act in corporate social responsibility. Corporations were required to disclose non-financial information for the first time in 2018 for the previous financial year. The conclusion of the European Green Deal and the Commission's Sustainable Finance Action Plan has further increased the need for companies to provide information on the sustainability risks they are exposed to and their impact on people and the environment. The COVID pandemic has further exacerbated the gap between disclosed and required data.19 To improve sustainability reporting, the Commission has proposed a new Corporate Sustainability Reporting Directive (CSRD). In this paper, we review the current practice in non-financial reporting in the EU and present the main highlights of the new CSD. With its requirements for additional reporting, auditor assurance on the reliability of sustainability reporting and sanctions, the new CSD also brings about greater accountability of management and supervisory bodies and consequent (positive) changes in corporate governance.

Key words: CSRD, NFRD, corporate governance, non-financial reporting, sustainability reporting, socially responsible corporate governance.

1. Introduction

We live in very restless times. The world had not yet recovered from the COVID-19 epidemic when a new crisis emerged due to the war in Ukraine. Although shocks such as these have occurred throughout human history, modern-day crises arise with ever shorter intervals. In these circumstances, the society and the economy have faced and will have to continue facing challenges brought by an uncertain future.

Companies' reporting on their operations coincided with the emergence of the global economic crisis of 2006, which broke out in the USA after the crash of financial giants, and then spread to Europe. As part of the measures aimed at restoring the lost trust of the capital markets and the general public in the companies' financial statements and reports, Directive 2006/46/EC introduced a corporate governance statement as a component of annual (management) reports. Directive 2014/95/EU on non-financial reporting (also known as the Non-Financial Reporting Directive, hereinafter: the NFRD) additionally introduced the obligation to disclose non-financial information for certain large undertakings and groups of undertakings (public-interest entities) in the form of a non-financial statement, which is substantively part of the management report, but can formally be presented as a stand-alone document. The purpose of the NFRD was to improve corporate social responsibility, which means undertakings should consider social and environmental issues when conducting their business and adopting strategies. Greater transparency of »non-financial information« can help companies to better manage non-financial risks and opportunities, thus enabling them to improve their non-financial performance (Bratina, Primec, 2017). After implementing the NFRD in practice, a positive correlation was identified between disclosing information pertaining to sustainable development and the assessment of undertakings by their stakeholders and capital market responses (Cho et al., 2021). Ever since the NFRD laid down the requirement to disclose non-financial information, when the latter was not merely voluntary, progress has also been noticeable in corporate practice (Aureli et al., 2021).

The European Commission responded to the growing demands for the management of new risks with a legislative package, which includes Regulation (EU) 2019/2088 of the European Parliament and of the Council on sustainability-related disclosures in the financial services sector (Sustainable Finance Disclosure Regulation), Regulation (EU) 2020/852 of the European Parliament and of the Council on the establishment of a framework to facilitate sustainable investment, and amending Regulation (EU) 2019/2088 (Taxonomy Regulation), proposal for a Directive on corporate sustainability due diligence (Corporate Sustainability Due Diligence Directive) and proposal for a Directive on corporate sustainability reporting (Corporate Sustainability Reporting Directive – hereinafter: the CSRD).

Applying the teleological method, this paper will present the theoretical background for non-financial reporting as the first legislative measure for more responsible corporate governance as introduced by the NFRD. We will discuss the legislative framework for non-financial reporting in Slovenia, in which the provisions of the NFRD are implemented, and, more specifically, the Companies Act (hereinafter: the ZGD-1). We will examine the effects of transposing the NFRD in the EU states and Slovenia by means of a study prepared for the Commission by the Centre for European Policy Studies (CEPS). We will focus on the new legislative proposal, the CSRD, which will thoroughly change the existing practice in non-financial reporting. We will ascertain whether the proposed changes are appropriate to improve the current practice that is being implemented based on the NFRD. In addition to the changes brought by the CSRD proposal, we will be especially interested in the effects of the new requirements on the management and supervisory bodies and, as a result, whether the new obligations will lead to more socially responsible corporate governance.

2. Theoretical Background

2.1 Corporate social responsibility

The purpose of introducing the institute of non-financial reporting was to ensure corporate social responsibility (hereinafter: the CSR).

Abrams' article published in *Harvard Business Review* in 1951 is often mentioned as the first paper on CSR, warning managers that they are not merely individually accountable to shareholders, but that they bear a wider social responsibility (Maak, 2008). From the initial idea of being accountable to the entire society (Bowen, 1953), the CSR evolved and was supplemented throughout the decades. From the inclusion of the legal responsibility of corporations, charity, ethics and ensuring legitimacy (Eels, Walton, 1974), the concept of CSR grew into Carroll's four-part model, which emphasised economic, legal, ethical, and philanthropic responsibility (Carroll, 1979). The CSR thus became much more fragmented and pluralistic, and probably fairer, yet too broad to encourage effective governance of corporate social responsibility (Maignan, Ferrell, 2004, Balmer, 2007). The latter refer to the assertions of Clarkson (1995) and others (Donaldson, Preston, 1995, Jones, 1995, etc.), (Maignan, Ferrell, 2004), stating that corporations are not responsible to the society as a whole, but only to those who directly or indirectly impact their activities or vice-versa. These stakeholders can be broken down into four groups (Henriques, Sadorsky, 1999): organisational (e.g., employees, customers, shareholders, suppliers), community (locals, special interest groups), regulatory (municipalities, regulative systems) and media. To this, Bucholz (2004) added another group: the natural environment.

When the Organisation for Economic Co-operation and Development (OECD) and European Union (EU) began becoming more deeply involved with CSR, it gained an international dimension (Carroll, 2008). The initial concept of social responsibility in the sense of »being good and charitable« significantly outgrew these outlines at the end of the 20th century, and established itself as an international standard of social responsibility (ISO standard 26000), (Primec, 2017).

2.2 Socially responsible corporate governance

Since corporate social responsibility falls under the remit of a firm's management and supervisory bodies, they must follow the requirements of responsible corporate governance in their related activities.

The theory of corporate governance began developing with Berle and Means' book *The Modern Corporation and Private Property* from 1932, in which the authors emphasised the separation of ownership and supervision as the central issue of modern corporate governance. This was the basis on which the first theory of corporate governance developed: the agency theory. Jensen in Meckling (1976) named the corporation the *firm*, which is a nexus of contracts, whose basic purpose is to maximise the shareholders' contributions. Two issues are important when it comes to governing corporations based on the agency theory: generating profit for the owners and resolving conflicts between principals and agents. As the corporation is merely a nexus of contracts, the interests of owners and the society are the same. Interests of other groups (workers, creditors, suppliers, etc.) were not taken into account in the governance, as they were protected by legislative and other rules. The agency theory became the dominant theory, which spread beyond the USA and worldwide, but not to a great extent, especially due to the differences in legal and cultural systems, as it is based on a series of hypotheses that are not compliant with the existing legal and institutional frameworks (e.g., shareholders own the corporation, a corporation does not have a legal personality, the competences of managers are determined contractually, not by law) (Magnier, 2017).

In parallel with this model of corporate governance (i.e., the shareholder primacy model), which is today named the economic model of agency theory, an alternative model of corporate governance began developing in the USA, one that is based on Dodd's doctrine, according to which managers were trustees for the corporation as a whole and, therefore, accountable to stakeholders within and even outside the company (Dodd, 1935). Dodd raised the theory of autonomous personality, pointing out that corporations have their own interests and social roles. Advocates of Dodd's doctrine put to the forefront corporations in which the elected managers would have the duty to fairly distribute the undertaking's assets among various interest groups. This was the basis for the development of the stakeholder governance model, also known as the stakeholder view, i.e., the stakeholder/legitimacy theory. This theory was introduced by Freeman (1984), who asserted that companies are accountable to a wide circle rather than just to traditional stakeholders. The stakeholder theory was greatly contributed to by Blair and Stout (1999) with their team production theory of corporate law.

The more recent series of organisational theories promotes sustainable corporate social responsibility, which places undertakings into a wider social and environmental context, encompassing the environmental, social and governance (ESG) criteria, thereby shifting the expansion of responsibilities of undertakings to the most advanced level.

The EU understands the CSR as a process in which companies must identify, prevent, manage and mitigate all negative impacts they may cause to the entire society (including the impact on human rights, health, the environment, global supply chains, etc.). The term of responsible business conduct (RBC) established itself as a synonym (European Parliament, 2020).

3. Non-financial Reporting as a Legal Measure for Greater Socially Responsible Corporate Governance

3.1 Content of non-financial reporting

Internationally speaking, there are many initiatives of the UN, the OECD and the International Labour Organization, emphasising the duties of undertakings to act responsibly and respect human rights. The 2000 United Nations Global Report in particular encourages undertakings to conduct their business responsibly based on the ten principles relating to human rights, labour, the environment and anti-corruption. In addition, it supports undertakings in adopting strategic measures that pursue wider social objectives, such as the sustainable development objectives from the UN 2030 Agenda.

In the past decade, the EU encouraged undertakings to conduct their business responsibly through optional and mandatory provisions intended to promote social responsibility. The most important legal act in this respect is the NFRD.

The NFRD imposed a requirement for disclosure of certain non-financial information of a company in the form of a non-financial statement (also known as a statement on non-financial operation) and a requirement for disclosure of information on the diversity of the members of administrative, management and supervisory bodies of companies (diversity policy). Both the non-financial statement and the description of the diversity policy within the corporate governance statement are a component part of the companies' management report. It should be noted that both in the doctrine and institutional circles, the handling of non-financial reporting is usually limited to the non-financial statement, while the diversity policy is not mentioned, which is why it will only be presented briefly in our paper.

The Companies Act (ZGD-1) stipulates that only large companies that are public-interest entities and whose average number of employees is greater than 500 on the balance sheet cut-off date shall prepare **a statement on non-financial operation** (the first paragraph of Article 70c of the ZGD-1). Entities liable to prepare a statement on non-financial operation include companies that are required to prepare a consolidated annual report and whose average number of employees exceeds 500 at the consolidated level (the twelfth paragraph of Article 56 of the ZGD-1). Directive 2014/95/EU specifically stipulates that small and medium-sized companies are exempt from this obligation, and the ZGD-1 follows the same line.

The statement on non-financial operation contains information that is necessary to understand the development, performance and position of a company, as well as the effect of its activities. To meet these criteria, the statement must include at least information on environmental, social and employee matters, respect for human rights and anti-corruption and bribery matters. In addition to the above, the statement must also include a brief description of the business model, a description of the company's policies regarding the above-mentioned issues, including the performance of due diligence procedures; the results of those policies, the main risks regarding the aforementioned issues in connection with the activities of the company, including its business relations, products or services where appropriate and proportionate, when these risks could cause serious damage in these areas, and the ways in which the company manages these risks, and key non-financial performance indicators which are important for specific activities (the first paragraph of Article 70c of the ZGD-1). This information relates to the past period of operation.

The **diversity policy** refers to the representation in the management and supervisory bodies in terms of gender, age or education, and the indication of goals, the way in which the policy is being carried out and the results of the diversity policy in the reporting period. If no diversity policy is being carried out, the company shall explain the reasons as to why (point 7 of the fifth paragraph of Article 70 of the ZGD-1). Information on a company's diversity policy is a component part of the governance statement. To this end, this information must be disclosed by all companies that are obligated to prepare a governance statement, i.e., companies that are obligated to carry out annual report audits (except medium-sized companies) and companies that must prepare a consolidated annual report.

Although the set of non-financial information is legally prescribed, companies are allowed a high level of discretion when deciding which information to disclose. If the company does not carry out any of these policies (environmental, social, employee, etc., including the diversity policy), it shall explain this in a clear and well-reasoned way in the statement on non-financial operation. When it comes to disclosing non-financial information, the EU has decided to take a »soft« approach and applied the »comply or explain« method, which was first introduced in the Cadbury Code (University of Cambridge, 2014).

3.2 Obligations of management and supervisory bodies

The NFRD has also determined the duty of management bodies concerning the preparation and adoption of annual reports, including the obligation to confirm them by means of their signatures, while the responsibility to prepare and publish financial and consolidated financial statements as well as annual reports and consolidated annual reports was left to be regulated by the member states.

In accordance with the Slovenian corporate law, the preparation and publication of information on non-financial operation, both for the governance statement and the statement on non-financial operation, is the responsibility of the members of the company management and supervisory bodies. Both documents are component parts of the management report, and the latter is part of the annual report, whose drawing up and publication is the collective duty of the management and supervisory bodies as arises from the first paragraph of Article 60a of the ZGD-1. Although their responsibility is defined by the general provision under Article 263 of the ZGD-1, which defines diligence, obligations and liability of the management and supervisory bodies, the responsibility for the drawing up and publication of the annual report with all its component parts, including the corporate governance statement and statement on non-financial operation (the latter was additionally included under Article 60a as a result of implementing the NFRD) was particularly emphasised as required by Directive 2006/46/EC. The specific emphasis on both statements in the text of the cited article and the further obligation imposed on the members of the management that the »annual report and its components shall be signed by all members of the company's management« from the second paragraph of Article 60a of the ZGD-1 indicate the importance of both statements and that of the information contained in them.

Upon publication, the relevant information on a company's operations become available to the general public, and thus members of the management and supervisory bodies carry an even greater burden of responsibility to provide »a true and fair view of the assets and liabilities of the company, its financial position and profit or loss« (the first paragraph of Article 61 of the ZGD-1) (Bratina, Primec, 2017).

4. Implementation of Non-financial Reporting in Practice

4.1 General information about the study on the NFRD

The NFRD is intended only for certain large companies. It does not stipulate common standards of reporting, which makes it impossible to make comparisons and thus prevents competition amongst firms in this field. It can, however, be used voluntarily by all companies (even small and medium-sized ones). Although the NFRD provisions enable a certain degree of flexibility, they do not stipulate clear and specific legal obligations that would apply to all undertakings regardless of their size. National legislations in particular do not determine the general tasks and duties that the management boards of all companies would have to take into account in order to prevent, quickly identify and mitigate the risks concerning human rights and environmental abuse in their undertakings, subsidiaries and throughout their supply chains. Similarly, initiatives in member states do not determine enforcement mechanisms and legal remedies for victims of irregularities committed by firms, or prescribe non-compliance sanctions, and so CSR remains, to a large extent, a voluntary initiative (European Parliament, 2020). These are the general findings that emerged from the short period of using the NFRD in practice. For a detailed analysis of the situation in non-financial reporting, the Commission has commissioned an extensive Study on the Non-Financial Reporting Directive in all 27 member states. The study analysed data on more than 17 million companies, gathered survey responses from more than 200 companies and conducted interviews with over 60 stakeholders (European Commission, 2020).

The NFRD is applied by around 2,000 companies. In practice, there are approximately 10,000 additional companies that are obliged to prepare non-financial statements based on broader transposition of the NFRD into national legislation. There are a further estimated 9,000 other non-public interest entities reporting without a legal requirement. The figures do not include subsidiaries.

Below we highlight some of the key findings (relevant to our topic) from the final report, as a detailed presentation (e.g., the cost aspect of non-financial reporting, etc.) exceeds the framework envisaged for this paper.

4.2 Scope of reporting in terms of the double materiality of non-financial information

As regards the scope of non-financial reporting in individual member states, the study highlights the issue of information materiality. The NFRD does not define this term. Although Commission guidelines on non-financial reporting from 2017 and 2019 point towards a more detailed definition, they do not provide a clear answer. This can cause differences in disclosing non-financial information in terms of double materiality. The criterion of double materiality differentiates non-financial information from the financial aspect (the outside-in perspective), whereby this is information that is relevant for the financial position and other performance indicators that are of special interest to investors, and the information from the environmental and social aspects (the inside-out perspective) concerning the impacts of the company on the environment and society in general, which are relevant to other stakeholders (citizens, consumers, employees, business partners, communities and civil society organisations (Commission Guidelines, 2019). Companies can therefore have a different understanding of information materiality, which consequently leads to differences in reporting on environmental, social and employee matters, human rights, anti-bribery and anti-corruption efforts. What is more, a question arises regarding the substantive disclosure of information, namely how is the disclosed information perceived by stakeholders, especially investors?

Research results show that 40% of the surveyed companies are aware of the double materiality of non-financial information, while 10% are unaware of it. In addition, around half of the companies place greater emphasis on disclosing information on the company's impacts on the environment (inside-out), while only 3% focus on the outside impacts on the company (outside-in). The double materiality of information was considered mainly by companies that are already sustainable and those who hire external advisors to prepare non-financial reports. The latter pointed out that disclosing financial and non-financial information in one single report would be the best approach to incorporate the concept of double materiality. This approach does not focus on the physical presence of information in a single document, but rather on the substantively uniform treatment and disclosure of information pertaining to the matters that have a short-, medium- and long-term impact on company value. The key challenge in this is that non-financial risks (environmental, social, governance, etc.) usually have a medium- to long-term impact, while financial reports only have a short-term impact (e.g., three to 12 months). Many of the smaller companies (41% of the total) report having more problems selecting which information is relevant, whereas this is only the case for 24% of the larger companies. Companies experienced with reporting, which they began implementing even before the adoption of the NFRD, also face fewer problems. For other companies, for which non-financial reporting is new, the difficulty of selection lessens over time and with experience. In the first year of reporting, selecting the information was difficult or very difficult for half of the companies surveyed, while the selection was neither difficult nor easy for 40%. In the following year of reporting, only 30% of the companies assessed the selection of the material information as still being difficult, while the share of companies with a neutral opinion rose to 50%.

According to the study results, reporting on non-financial information following the double materiality concept depends on the size of the company and its experience with reporting.

4.3 Impact of non-financial reporting on corporate governance

One of the research questions that is especially interesting for our paper was what impact does non-financial reporting have on a company's behaviour? In the study, changes in company behaviour refer to different organisational practices and management decisions:

- an increased awareness of non-financial issues;
- changes in internal procedures related to the production and approval of the non-financial statement (e.g., internal cooperation, greater recognisability of non-financial information);
- adjustments to internal policies and practices (e.g., energy consumption in offices);
- the integration of non-financial risks in the company strategy;
- changes in diligence processes and policies with a direct impact on the main business of a company (e.g., transition from fossil fuels to wind energy, abandoning business connections with companies that do not respect human rights).

These changes were detected over the past few years in numerous companies included in the research, but in different ways and in different scopes. The study explicitly points out that it is difficult to disentangle to what extent those changes are attributable to the NFRD or other factors, like the demand from business partners or stakeholder expectations (European Commission, 2020, p. 112).

What's most important is that due to the requirements for non-financial reporting, companies noticed an increased awareness of employees and management bodies regarding non-financial risks, impacts and opportunities. In addition, better engagement of stakeholders and employees was identified at all levels, along with deeper coordination and communication across departments and units, as well as the establishment of appropriate bodies within the company. Efforts directed towards the long-term vision and deeper integration of sustainability in the company strategy were enhanced, internal risk management systems were re-evaluated, etc.

About one-third of the companies estimated that the non-financial reporting obligation had little to no impact on company practices. This information is not surprising and does not go against the previous finding, as it mainly concerns companies that already had non-financial reporting in place before the NFRD or whose reporting was driven by national requirements. Some companies estimate non-financial reporting as an additional administrative burden without clear additional benefits, or attribute the main reason for any sustainability action to demands from customers and investors, which was absent for some respondents.

4.4 Common conclusions

The final report suggests that the NFRD requirements for non-financial reporting have resulted in an increased awareness about the significance of non-financial information. The scope of disclosed non-financial information increased as well. This has clearly been the case in Germany, Italy, the Netherlands and Spain. Preparing reports, which have to be submitted and approved by the management bodies, resulted in more cross-departmental cooperation, especially in determining the right (material) information. Changes of this kind are less visible for companies that already reported non-financial information before the implementation of the NFRD, where the management already exhibited a certain sensibility to non-financial matters and internal procedures, and where structures for reporting were in place.

Furthermore, changes induced by the NFRD appear less important in countries where the culture of non-financial reporting is still not very developed and very few companies are under its scope (the Czech Republic, Estonia, Hungary and Slovenia). In these countries, according to various stakeholders, non-financial reporting is sometimes perceived more as a communication exercise than a strategic document reflecting the company's approach to sustainability.

While most companies claim that through the NFRD a better integration of non-financial risks was achieved, this statement does not fully match the perception of key stakeholders, like business associations and investors. For them, such an integration is not visible, or only applies to climate risks. In addition, based on their understanding, a better integration of non-financial risks cannot be connected to the NFRD (European Commission, 2020, p. 114).

5. New Features Brought by the CSRD (Development of Non-financial Reporting De Lege Ferenda)

As the results of the Commission's 2020 study on the NFRD suggest, the non-financial reporting obligation has forced companies to begin thinking about the non-financial risks they encounter in their operations in a more systematic and comprehensive manner, which has led to changes in company strategies and to a different, more socially responsible form of governance. However, according to detailed interviews with the stakeholders, these changes are not sufficiently recognisable or refer only to certain non-financial risks, which is not enough for a comprehensive insight into the non-financial operations of companies, which is especially important for investors and business partners. Doctrinal views are similar. They point out the limited effects of the NFRD in terms of the transparency of non-financial reporting, assurance, comparability of information and business models (Nicolo et al., 2020, Venturelli, Pizzi, 2020). By contrast, the need for high-quality information on risk management in companies, which arises from the increasingly uncertain political and, consequently, economic and social contexts in which firms operate, is increasingly relevant and necessary.

The above reasons (and many others not included in the paper due to its limited scope) have led to legislative changes in sustainable corporate governance (presented in detail in the introductory part of the paper). Below, we will limit our focus to presenting certain crucial changes brought by the CSRD proposal, which is changing the NFRD as well as the Accounting Directive 2013/34/EU and Directives 2004/109/EC and 2006/43/EC. We start by noting the weaknesses of the currently applicable NFRD, and then examine the changes that have been proposed to address these.

5.1 Expanding the circle of information that needs to be disclosed

Companies must disclose information pertaining to five areas: business model, policies (including the implemented procedures of due diligence), results of these policies, risks and risk management, and key performance indicators that are relevant for individual activities.

Companies are not required to refer to other areas of reporting, which would reveal the their resilience to risks relating to sustainability. The CSRD proposal stipulates that, in addition to the information already required, companies should be required to disclose information about their business strategy and the resilience of their business model and strategy to risks related to sustainability matters; any plans they may have to ensure that their business model and strategy are compatible with the transition to a sustainable and climate-neutral economy; any opportunities for the undertaking arising from sustainability matters; the role of the management and supervisory bodies with regard to sustainability matters, etc. (for details, see the new Article 19.a entitled Sustainability Reporting)

5.2 Reporting obligation and standardised reporting method

The current legislation requires companies to consider double materiality, and not to report only on the information »to the extent necessary for an understanding of the undertaking's development, performance, position«, but also on information necessary for an understanding of the impact of the undertaking's activities on environmental, social and employee matters, respect for human rights, anti-corruption and bribery matters. Firms are therefore required to report both on how various sustainability matters affect the undertaking, and on the impacts of the activities of the undertaking on people and the environment, which is understood and implemented differently in practice.

Further, information on individual company policies is disclosed in line with the »comply or explain« method, which causes confusion and does not ensure high-quality information. Companies can use various reporting frameworks for their disclosures, either national or international (GRI, EMAS, etc.), which makes it impossible to compare them. To simplify and unify non-financial reporting, the Commission has adopted guidelines on non-financial reporting, but these are not mandatory and have, in practice, not contributed substantially to the higher quality of non-financial reporting.

These factors have resulted in a conclusion that non-financial information should be disclosed in a unified manner that is binding for all companies in order to ensure comparability and disclosure of all the relevant information. The CSRD proposal therefore introduces reporting standards to be adopted by the Commission with the expert support of the European Financial Reporting Advisory Group (EFRAG) in the form of delegated acts. The standards will have to take into account the principle of double materiality and encompass all the relevant information. The standards are necessary for comparability among companies, and for easier adoption of business decisions as regards impacts on sustainable development (ECIIA, 2021). Mandatory common standards will enable an in-depth review (assurance on the reliability of sustainability information) and digitisation of reporting (digital taxonomy of the EU's standards for reporting on sustainability). The aim of introducing common standards is to progress to a situation in which non-financial information has a status comparable to that of financial information (the CSRD proposal, point 32 of the introductory part).

To ensure the provision of quality and necessary information, the sustainability report will be part of the management report, and it will no longer be possible to publish it as a separate document. After the CSRD has taken effect, it will be possible to present the diversity policy, which has thus far been included in the governance statement, within the sustainability report (the new Article 19c of the CSRD proposal).

5.3 Sanctions

The NFRD has left the determining of sanctions concerning breaches of the obligation of disclosing non-financial information to the member states. As mentioned in section 3, in Slovenia the drawing up and publication of a statement on non-financial operations is the responsibility of members of the management and supervisory bodies. The ZGD-1 also explicitly states that the statement must be signed by all members of the company's management (Article 60a). If the annual and management reports do not contain all the mandatory elements, or if the annual report is not signed by all the members of the company's management, these are regarded as offences which the ZGD-1 in points 8, 9 and 10 of the first paragraph of Article 686 defines as offences for which a sanction is imposed on the legal entity and its liable person.

The CSRD proposal introduces a unified system of sustainability reporting, which consequently requires the unification of the system of sanctions pertaining to it. That is why the minimum types of sanctions are now specified, which member states should provide for in the case of infringements of the national provisions transposing the sustainability reporting requirements of the Accounting Directive: a public statement indicating the natural person or the legal entity responsible and the nature of the infringement; an order requiring the natural person or the legal entity responsible to cease the conduct constituting the infringement and to desist from any repetition of that conduct, and administrative pecuniary sanctions. Member states shall ensure that, when determining the type and level of penalties or measures, all relevant circumstances are taken into account, such as the gravity and duration of the breach, the degree of responsibility of the natural person or legal entity responsible, etc. (for details, see the third paragraph of the new Article 51 of the CSRD proposal).

6. Conclusion

corporate social responsibility unquestionably remains an increasingly important aspect of successful modern governance, without which it would be impossible to imagine corporations functioning in the near future. Moreover, now no longer a peripheral part of company operations, CSR is becoming the key to success (Cho et al, 2021, referring to the Verdantix report). This is attested by changes to EU corporate law (as presented in the introduction), with consequent changes to the national corporate law of member states.

Sustainable management is the responsibility of the management bodies of corporations. What their responsibility will be and how they will manage sustainability risks depends on the regulatory (legislative) framework in which they operate. In this process, the legal aspect of the CSR is coming to the forefront, namely how to bind management and supervisory bodies through legal rules to socially responsible corporate governance. Legal CSR is the corporate duty of managers, binding them to not only act for the benefit of the company and shareholders, but also for the benefit of other stakeholders, for which they are also liable for damages (Bohinc, 2016).

Through socially responsible (sustainable) reporting, changes introduced by the CSRD and presented in detail in section 5 will also contribute to a certain extent to the strengthening of socially responsible corporate governance in the legal sense (with a precise set of information that needs to be disclosed; with the obligation to report on this information; on the method of communicating information – in the form of standards and in digital form, which will enable comparability of information; and with sanctions envisaged for companies and persons responsible for non-financial reporting).

The Commission's study on the NFRD and the doctrinal findings confirm that, in practice, non-financial reporting has increased awareness about the significance of non-financial information, and has led to shifts in corporate governance. We can therefore justifiably expect that mandatory standardised reporting in this field, along with other changes brought about by the CSRD proposal and its more specific rules, will serve to further strengthen corporate governance in terms of sustainable development.

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CORPORATE GOVERNANCE BETWEEN EFFICIENCY AND SOCIAL RESPONSIBILITY

Peter Svetina, Jože Ruparčič

Corporate social responsibility is essential to overcome the exclusivity of the principle of »maximizing the shareholder value« and excessive »financialization« of companies in order to put focus on a long-term horizon in terms of productivity growth, innovations and sustainable development, which should become the central characteristic of the innovative companies, based on knowledge. (Rado Bohinc)

Abstract

Corporate social responsibility (CSR) is a coherent force of modern entrepreneurship and is the right answer to today's challenges. CSR brings reassurance to society, as it advocates both free economic initiative and social responsibility for environmental, social and universal social issues. Above all, the social responsibility of entrepreneurs and business people is in their interest, as it raises awareness of the importance of their work and the contribution they make to the community. Their image is thus strengthened. So companies which accept CSR are more successful. These are positive synergies within society. CSR is the way of governance (societal and corporate) that takes into consideration social consequences of governance decision as equally important as economic ones (capital gain).

Key words: corporate social responsibility, society, free economic initiative, social consequences of governance

1. Introduction

The effectiveness of corporate governance and social responsibility are complementary and part of the same story. Entrepreneurs operate in the social space and are not excluded from this society. Therefore, they must be interested in working in a healthy, creative and social environment that they co-create. The businessman builds bridges between the various stakeholders of the organization and society. Due to their positions, roles and positions, the stakeholders of the organization have different, often very conflicting interests, needs and expectations. Owners and employees, financiers and buyers, partners and the local community, suppliers and unions point to sometimes distant views on what they would really expect from participating in or living in a particular economic organization. Therefore, a businessman must act preventively by treating all key stakeholders in his organization equally. This means he must patiently build strong bonds between them. Balanced attention to special practice and all together proves to be that masterpiece that ensures optimal well-being for all. With this, we gave another good reason in favour of the need for business ethics in everyday economic life. The focus on integrity in the business world must be at the core of the company, which is characterized by consistency in business decision-making, conduct, principles, expectations and results of operations. It is manifested individually in moral conduct, which is what business ethics serves. Integrity and honesty of governing bodies are postulates of good character and personal maturity in all known cultures and civilizations without exception. Very often we place them right on top of what constitutes the essence of personal, individual moral greatness. Honesty of directors is therefore often associated with the concept of conscience, and in this regard, honesty in the business world is basically guaranteed by a clear conscience. Therefore, integrity and honesty are also among the important goals of education, ie the formation of the individual and personality. Justice represents the necessary social basis for participation in the involvement of individuals in the processes of society, which requires their marginalization within modern society, which requires a detailed interdisciplinary approach. In terms of fundamental human rights, it means that everyone must be able to participate equally in social processes. Aristotle maintained the teacher's arc between reality and the ideal by redirecting it to the everyday coexistence of man in the polis. According to him, people do not coexist in the country to live together, but to create a good life. The polis has an inner purpose of existence, which manifests itself as a constant drive from lower to higher kinds of perfection of being. Thus, excellence and the need for it, through perfection in virtues, became the ultimate goal of human existence. We understand that social implications of governance are as relevant as economic. CSR in this respect is the responsibility for the social consequences of governance. Effectiveness of corporate governance and social responsibility go hand in hand.

2. Freedom and Enterprise

Free economic initiative is regulated by the basic Article 74 of the current Constitution. The Constitutional Court considers it in connection with the principle of legal certainty and trust in the law (Article 2), the prohibition of discrimination on the basis of personal circumstances (Article 14) and the general provision according to which entrepreneurship may be limited only by the rights of others. determined by the Constitution itself (paragraph 3 of Article 15). The intertwining of free economic initiative with property, corporate and management rights based on the right to private property and inheritance is obvious and strong (Article 33). Last but not least, free enterprise initiative also falls within the area of protection of general freedom of action, which derives from the inviolability of personal rights (Article 35). Free enterprise coincides with free economic initiative. By ensuring competition - the prohibitory norm of Article 74), the Constitution also recognizes the free market on the basis of fair and free competition as a fundamental principle of economic regulation. Competition enables free economic initiative and entrepreneurial freedom. Market constitutional law thus encompasses the whole set of rights from Articles 33 and 74 in connection with the free choice of profession and job (Article 49) and the protection of intellectual services (Article 60), taking into account the framework of general provisions on the rule of law, prohibition of discrimination (Article 14), permissible restrictions on rights (Article 15) and general freedom of action (Article 35). The European Convention on Human Rights protects free enterprise through comparable provisions on the right to association (Article 11 of the ECHR also protects the freedom of establishment), the right to property (Article 1 of the First Protocol) and the protection of civil rights (Article 6). As a rule, the EU Court of Justice infringements of free economic initiative together with the right to private property. Based on the jurisprudence of the Court of Justice of the EU, free economic initiative has been included among the fundamental provisions contained in the Charter of Fundamental Rights of the European Union (Article 16 of the Charter). The Constitutional Court of the Republic of Slovenia adopted the position that the rights to free economic initiative under EU law and the Slovenian Constitution are substantively and legally equivalent.[1]

The right to free economic initiative is a right of mixed status. On the one hand, it protects economic operators from state interference (U-I-296/96). It is therefore a right to defend and a negative status. On the other hand, it is an economic right and a right that cannot be exercised without legislative regulation (U-I-218/04). Moreover, the first sentence of the second par. and the third par. Articles 74 explicitly prescribe to the legislator that he must adopt the appropriate legal regulation. This indicates that this right is also a right of positive status, where an individual can request a certain activity from the state. Namely, the omission of the legislator could constitute an obstacle to the exercise of free economic initiative or an unconstitutional legal vacuum (U-I-173/97, item 6; U-I-16/98, item 15). If a law containing the basic rules of public order, insofar as they are essential for the market, is defined as »market constitutional law«, the provision of Article 74 is also part of this law. According to this thesis, this would also include provisions on the right to private property and its borders, on the free choice of profession and workplace, on the constitutionally guaranteed protection of intellectual services. The theory emphasizes that the Constitution, in its relation to the economic system of the state, in principle does not decide on its regulation, but on its freedom. However, the Constitution maintains a certain neutrality regarding concrete economic regulation, namely it allows the possibility of legal interference in it. That in the case of Article 74 the Constitution maintains economic neutrality is also evident from the emphasized public interest in this field (the second sentence of paragraph 2 speaks of public benefit). An important correction of the principled market orientation of the economic system is the principle of the welfare state (Article 2) and also the constitutionally guaranteed protection of (other) human rights. It is therefore necessary to assess that, in those frameworks, the legislature has broad powers to formulate economic policy and to take measures to attain the objectives of that policy. That the extreme liberal conception of entrepreneurship is not constitutionally consistent has been repeatedly emphasized by the US (eg OdlUS VI, 7, U-I-273/96, Ur. L. 13/97, item 4), as well as the need for a

1 Jambrek, 2018.

balance between economic freedom initiatives and social principles enshrined in the Constitution (eg OdlUS IV, 113, item 11).[2]

Understanding the importance of freedom and related business decision-making leads us to understand the importance of entrepreneurial activity and their impact on economic and social development. The central idea of the creators of the necessary social changes in the economic field must therefore be focused on a free, creative and ethically designed business environment. Exclusionary policy must not be enforced in any way, but the integrative synergistic effects of the complementarity of directors' actions must be in line with moral rules. Free and ethical business decision-making is closely linked to knowledge and wisdom. Directors act for the benefit of the company they run and at the expense of shareholders. This also means that they will use their knowledge and strengths carefully, conscientiously and prudently for the interests of the company. All with the awareness that they operate within a social environment that allows them to create added value. Therefore, it is in the interest of entrepreneurs that society is healthy and able to respond to the challenges of time and space.

3. Business Ethics

The role of business morality is precisely to indicate to the businessman what is worthy of human conduct. Seneca says, »Id facere laus est, quod decet, non quod licet.« This means: The quality is to do what is worthy, not just what is allowed. In the field of business morality, it is therefore necessary to develop the moral sense (moralis sensus) as an expression of the innate feeling for a businessman to distinguish between good and evil, natural and unnatural and reasonable in business. Of particular importance to business ethics is a moral sense built on rational effects that are supposed to promote what is morally good and reject morally bad in terms of relationships between people in the entrepreneurial race. It is not enough for the business world to develop not only a moral sense for

2 Komentar k 74. členu Ustave Republike Slovenije, Komentar Ustave Republike Slovenije, Nova Univerza, Nova Gorica, 2019.

establishing humane relations with fellow competitors in entrepreneurship, but also the presence of the benefits of morally acceptable business is necessary. The focus on integrity in the business world must be at the core of the company, which is characterized by consistency in business decision-making, conduct, principles, expectations and results of operations.[3]

It is important that managing authorities are aware of their impact on the community from an ethical point of view when making business decisions. Entrepreneurship, as the most common form of business life, imbued with ethical norms and values, is a state in which entrepreneurship meets the highest standards and requirements of people for humane, fair and humane conduct in professional life. Entrepreneurs are increasingly aware of the urgent need to comply not only with applicable legal and other legal business rules and autonomously designed standards and customs, which in practice are formed as business and good business practices, but also with the need to strive to enforce higher moral and ethical standards in business. Entrepreneurs are also aware that economic operations must be subordinated to higher standards, which help to create entrepreneurship as an upright humane personality through entrepreneurship, and that exchange and sharing fairness in the field of economy is also being enforced in the business world. is the minimum of ethical evaluation of business.[4]

Forma mentis of entrepreneurial activity must represent ethics and fairness, which are the appropriate basis for making business decisions. A keen sense of fairness in making business decisions, which, in accordance with the principle of diligence and honesty, implements the logic and vitality of the concept of ethics in law.

Entrepreneurs must be aware that business operations should be subject to higher standards, which help to create entrepreneurship as an upright humane personality through entrepreneurship and that exchange and sharing equity in the field of economy is also enforced in the business world, which is the minimum of ethical evaluation of business. The theory highlights five ethical starting points that should guide us in making business decisions:[5]

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3 Ivanjko, 1997, page 11.

4 Right there.

5 Glas, 2003, page 10.

1. The decision should be useful, it should achieve the greatest possible surplus of benefits over losses, burdens (the principle of utilitarianism).
2. The decision should be based on honesty, equality and impartiality, it should not be unfair to any participant.
3. Fundamental human rights must be respected, including freedom, equality of dignity and the rights of all people, and there must be no discrimination.
4. The decision must be acceptable to the members of the organization (of course to rational, reasonable individuals), which they must make.
5. The decision must be permanent, valid for a longer period; under sufficiently changed circumstances, a different decision may be made.

As a moral being, man will never come to terms with his imperfection and the imperfection of the world in which he lives. His thinking and acting throughout the history of Western European civilization took place as a project of conscious mastery of the world of life through intellectual and moral perfection in order to achieve universal excellence.[6]

4. Corporate Social Responsibility

The operation of governing bodies in accordance with moral rules is the raison d'etre of the code of ethics of every responsible director and puts the social syntagm of integration into the business environment within the framework of the best and best that each nation has from the national economic point of view. The concept of CSR should not be understood only as an aid in creating the external image of a company, although most companies have recently used it precisely because of public relations. CRS means that companies not only strive for the highest possible revenues and profits, but also that they include respect for and promotion of human rights and care for the environment in their operations. Social responsibility

6 Jelovac, 2010, pages 83–100.

requires companies to consistently respect and fulfil their legal obligations, because in the internal and external environment they must actively promote and support respect for the respective constitutional order. The fact that the issues of CSR towards human rights, prevention of corruption and environmental protection are becoming more and more important is evident from the data that many domestic and international companies attach increasing importance to society's attitude towards employees and the wider community.[7]

Social responsibility is the way of governing a society or a corporation following social objectives in addition to the economic development on societal level or maximization of profit on corporate level. Social responsibility is the way of governance (societal and corporate) that takes into consideration social consequences of governance decision as equally important as economic ones (capital gain). We understand that social implications of governance are as relevant as economic. Social responsibility in this respect is the responsibility for the social consequences of governance. Social responsibility is the way how members (individual or corporate) of the society or stakeholders of a corporation, should behave and perform their activities, as to maintain coexistence with other members of society and with society at large Social responsibility refers to all members of the society, be it individual or corporate. There is no difference in the duty of socially responsible behaviour. The difference appears, when we talk about social responsibility as an ethical commitment. When talking about social responsibility on global level, every entity, doing activities in an intercourse with nature shall maintain balance between the economy and the ecosystems. In addition, a balance should be searched between the profit and social well fare or, to say broader, between economic and social development. A trade off shall be achieved between two desirable but incompatible features; or to be less ambitious, at least a compromise (in search of equilibrium). New social responsibility is an innovative theoretical approach to societal and corporate governance. Social responsibility at societal level, also referred as country social responsibility, is the ability of an individual country's legislation to ensure a high level of social wellbeing, economic and environmental sustainability, without further deepening income inequalities and violating human (economic and social) rights. Out of the

7 Letnar Černič, 2009, page 9.

three pillars of sustainability - economic, environmental, and social, this paper refers only to social, considering it, as equally important as economic and environmental. Social responsibility on corporate level is the attitude that creates opportunities to empower people to become main actors and beneficiaries in the enterprises they work.[8]

Gilliand and Langdon presented some tips for improving employee efficiency and the business environment:[9]

– consistency in all steps and stages of the process;
– evaluation should be based on work-related factors, as it is not biased;
– employees should be given the opportunity to challenge and discuss the correctness of the evaluation and the assessment made;
– all aspects of the process should be discussed with employees;
– feedback should be timely and informative;
– employees must be treated with respect;
– make sure that employees are not surprised by the outcome (positive or negative).

CSR should be considered as a specific business culture, with business behaviour that goes beyond legal requirements being accepted voluntarily because the company believes it is in their long-term interest. It is linked to the concept of sustainable development: companies need to include awareness of their economic, social and environmental impact in their operations. Nor can it be an alternative to business activities, but a way for companies to be run. This way of doing business should have a positive effect on the competitiveness of companies, especially with regard to the awareness of consumers and financial investors about the image and reputation of companies. In addition, CSR may be required for companies operating abroad, for example in developing countries; Namely, financial institutions and investors also take into account activities related to CSR when assessing the positive aspects and risk factors that are part of the company. Namely, governance is socially responsible, devoting part of economic growth at the level of the national economy to social well-being, a better life for people and social

8 Bohinc, 2019 [upcoming book].

9 Gilliland, Stephen W.; Langdon, Jay C.,1998.

development. Social responsibility is therefore responsibility for the social consequences of management at the state or corporate level.[10]

Ban Ki-moon, Secretary-General of the United Nations, said in 2013: »Sustainable development is the path to the future that we wish for all. It provides a framework for creating economic growth, achieving social justice, implementing environmental governance and strengthening governance.« Our understanding is that CSR includes the perception that sustainable business success and shareholder value cannot be achieved by maximizing short-term profits but market-oriented but responsible behaviour. Businesses are aware that they can contribute to sustainable development by managing their business by increasing economic growth and competitiveness while ensuring environmental protection and promoting social responsibility, including consumer interests. In line with this understanding of CSR, the integration of social and environmental issues into companies is voluntary, with the aim of promoting business goals. Companies voluntarily include social and environmental issues in their business, rather than understanding it as their responsibility. This is a fundamental misunderstanding in the interpretation of CSR. The phrase 'CSR' is misleading, as society does not take on social responsibility. In principle, it is a market-based instrument that enables companies to do charity and other activities aimed at creating and raising awareness of the good reputation of companies. CSR means that someone is responsible for the social, environmental and economic consequences of their actions; this means that it also bears the potential burden of its economic activity in the social and environmental spheres.[11]

CSR means »decisions and measures taken for reasons at least in part beyond the direct economic or technical interest of the company«. McGuire extended this definition by arguing that companies not only have economic and legal obligations, but are also socially responsible and thus go beyond those obligations. Others have more comprehensively defined CSR as the company's obligation to use its resources to benefit society by participating as a member of society. Social responsibility therefore includes the voluntary acceptance of principles, processes of social responsiveness and tangible results of social relations. Regardless of the definition of business strategy and

10 Bohinc, 2016a, page 177.

11 Right there.

CSR activities used, which simultaneously meet the current needs of companies and stakeholders, companies should simultaneously protect, conserve and strengthen the human and natural resources that humanity will need in the future, which means serious consequences for them (IIA, 2010). Social responsibility applies to all members of society and is the way in which members of the community (individuals or legal entities) of the company behave and perform their activities in order to maintain coexistence with other members of society and society in general.[12]

Black and Quach (2009) highlight the benefits of socially responsible entrepreneurship, which has a synergistic impact on business performance:[13]

– Responsible CSR practices can improve risk management in the company and provide appropriate strategies and measures to reduce risk.
– Tailoring CSR issues can create value by helping companies identify and develop opportunities for new products and or markets.
– Improved alignment of CSR with the company's overall strategy can reduce operating costs by improving operational efficiency and exploiting scarce resources.
– CSR initiatives can encourage the learning and innovation of employees and companies by exploring new ways to do the same things better or behave differently.
– CSR can enhance the reputation of companies and brands through communication with external customers. This creates a positive image with customers, investors, bankers and supporters. A great reputation encourages sales, and a loss of reputation also means a loss of customers.
– CSR strategies can help companies improve employee motivation while maintaining and attracting quality staff.
– CSR can help companies develop new competencies, resources and capabilities.
– Failure by companies to take into account their impact on society and the environment may lead to the withdrawal of their operating or metaphorical operating licenses.

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12 Ackers, 2014, page 39.

13 Ackers, 2014, page 39–40.

– CSR can facilitate access to capital, as capital markets are increasingly affected by risk assessments based on the environmental, social and managerial dimensions of the company.

As societal values and expectations change, dynamic concepts such as CSR continue to evolve and adapt to changing societal norms. Despite widespread acceptance, effective corporate practices are limited by an inadequate normative basis for effective regulation.14 The concept of social responsibility has previously been linked to the alienation of profits, and modern business leaders recognize the important role of charity, also because CSR can be an investment in increasing shareholder value and business success.[15]

14 Ackers, 2014, page 40.

15 Lord Goldsmith, Lords Grand Committee, 6 February 2006, columns 255–258, Hansard: »What is success? The starting point is that it is essentially for the members of the company to define the objective they wish to achieve. Success means what the members collectively want the company to achieve. For a commercial company, success will usually mean long-term increase in value. For certain companies, such as charities and community interest companies, it will mean the attainment of the objectives for which the company has been established … For a commercial company, success will normally mean long-term increase in value, but the company's constitution and decisions made under it may also lay down the appropriate success model for the company … it is essential for the members of a company to define the objectives they wish to achieve, the normal way for that to be done – the traditional way – is that members do it at the time the company is established. In the old style, it would have been set down in the company's memorandum. That is changing … but the principle does not change that those who establish the company will start off by setting out what they hope to achieve. For most people who invest in companies, there is never any doubt about it – money. That is what they want. They want a long-term increase in the company. It is not a snap poll to be taken at any point in time … it is for the directors, by reference to those things we are talking about – the objective of the company – to judge and form a good faith judgment about what is to be regarded as success for the members as a whole … they will need to look at the company's constitution, shareholder decisions and anything else that they consider relevant in helping them to reach that judgement … the duty is to promote the success for the benefit of the members as a whole – that is, for the members as a collective body – not only to benefit the majority shareholders, or any particular shareholder or section of shareholders, still less the interests of directors who might happen to be shareholders themselves. That is an important statement of the way in which directors need to look at this judgement they have to make.«

Corporate social inclusion has evolved from simple financing of 'important things', 'booklet philanthropy' to strategic CSR, with CSR activities being more in line with the company's expertise and skills. Although the discourse on CSR has been present since at least the 1930s and despite the growing awareness of companies about their social responsibility, it is clear that companies' efforts to fulfil their social responsibility have not yet reached a tipping point. CSR is a growing, dynamic movement which is gaining respect among the younger generation of tomorrow's tech and business leaders as well as with long existing, publicly-held corporations. These leaders don't talk about shareholders; they talk about the community; they talk about growth; they talk about sustainability. The idea of social entrepreneurship was born in the early 1990s when »a handful of wealthy executives and investors, most of them connected in some way to the budding tech boom, began to think about how philanthropy might work [differently and] about how they could take what made them rich in business and apply those tactics to charity.«[16]

5. Corporate Social Responsibility and Environmental Impact

Government policies also influence business decisions - through regulatory mechanisms, property rights and responsibilities, disclosure powers, taxes and subsidies, procurement criteria and other policies - but are primarily business initiatives in the field of environmental protection. The role of environmental aspects in business decision-making has been seriously underestimated in the past. Environmental research has been based on the natural and health sciences and engineering, which addresses issues such as the health risks of individual substances, the functioning of environmental processes and ecosystems, the effects of change on them and the development of pollution control technologies. Environmental research in the social sciences to date has focused mainly on economics, including measuring the economic costs and benefits of

16 Ackers, 2014, page 40.

pollution control and the relative effectiveness of regulatory powers and market-oriented environmental policy instruments, government decisions, and less on environmental decisions of individuals and households are energy saving, recycling and environmental aspects of consumer behaviour.[17]

When does it pay to be »green«? The most important issue relates to the conditions under which business decisions that strengthen the environment also increase competitive advantage and other business objectives. The answers to this question are essential for the environmental decisions of both companies and governments, who choose between regulatory and more market-oriented incentives. If environmental protection brings a market advantage, does such an advantage stem primarily from external incentives such as customer or investor demand, government demands and subsidies, or pressure on society and the community? Or does it also stem from the distinctive capabilities and resources of the company itself, as a growing body of business research shows? Further research is needed to describe in more detail why some facilities and companies create a greater competitive advantage through better environmental performance than others, also in the same sector, and to identify how this is affected by internal capacity and external pressures.[18]

How do the competitive advantages of environmental protection, if they exist for individual companies, affect environmental protection? Are these practices gradually spreading to other companies, which reduces the initial competitive advantage of the first companies but improves the overall environmental performance? Do successful companies use their competitive advantage to gradually replace poorer competitors according to Schumpeter's theory of creative destruction? Or do successful companies gain their competitive advantage only through top-notch niches, and poorer operators continue to coexist with them in other markets and with less overall improvement in environmental performance? To understand the overall environmental impacts of corporate safeguards, it is essential to understand not only the behaviour of the most innovative and competitive companies, but also their impact and the limitations of this impact on the environmental performance of other companies. Entrepreneurs can do good business and create effectively only in

17 National Research Council, 2005, page 52.

18 Right there.

a healthy and clean environment. A healthy environment increases the efficiency of companies, which is conditioned by CSR.[19]

6. Social Enterprise

Human relations in the community, ethical and moral principles, co-management, co-responsibility, culture of cooperation, intergenerational solidarity, are expressions that evoke positive emotions in us and are appropriate and relevant in every period, not only today, when we face the ubiquitous crisis. Although we are looking for answers to the positive and even development of society in all periods of social and personal life and living, today their importance is especially emphasized. Sustainability in all segments, especially in the business world, is a challenge we face and seek answers to.

Recently, there has been a lot of talk in Slovenia, Europe and globally about social entrepreneurship, which is supposed to respond to the crisis of values and goods and ensure a fairer society, a stable economy and a high social standard. In Slovenia, the term social entrepreneurship is more often used, but it is more appropriate to talk about social entrepreneurship, as it is primarily entrepreneurship that is aware of its responsibility to social phenomena in the broadest sense and responds to them in an entrepreneurial way, not just solving social problems as is often misunderstood. In the last period, classical entrepreneurship has only the connotation of accumulating profit for individual interests and disposing of it in a way that is not sustainable and is only short-lived. A look at history and also at modern companies that operate on the principles of socially responsible behaviour shows us that successful companies are only those that prudently manage their profits and invest them in their development, while investing in the development of their physical and social environment in which they operate.

In Europe and Slovenia, the debate on social entrepreneurship has revived awareness of the values we have lived since the beginning of the cooperative movement, genuine human relations, intergenerational coexistence and solidarity. Concepts such as cooperatives

19 Right there.

(savings banks, agricultural, housing ...), investing profits in the development of the company, solving environmental issues, etc., have accompanied us for generations.

Self-sufficiency of the population is certainly one of the most pressing topics at the moment, and social entrepreneurship is certainly a possible answer to it. Connection between producers and consumers, not only in the form of production – consumption but on the joint assumption of responsibility for production and, last but not least, consumption, is the basis for responsible and quality cooperation and, consequently, self-sufficiency. Integrating into appropriate forms of association (various forms of so-called social enterprises), observing ethical and moral principles, optimizing and reinvesting profits in production and development, ensuring optimal relationship between quality and price are the ways to respond to this burning topic. Offering solutions in the field of self-sufficiency of the population is a challenge that we must tackle consciously and with a great deal of responsibility. The field itself offers entrepreneurial challenges, but they must be sustainable. Processing, production and consumption call for responsible behaviour and networking of all stakeholders who are willing to be actively involved in the processes. Equal participation of all stakeholders in the process, acting on agreed, ethical and moral grounds, respecting the principles of social responsibility and awareness of their role in the chosen circle are the basics that each stakeholder must be aware of and committed to when entering the process. Establishing self-sufficiency and the principle of »short chains« satisfies the needs of various stakeholders and significantly increases their satisfaction with services, as well as increases the quality of the food itself. It is distinct that we are covering all sections of the population, including our children. It is also important that each of the stakeholders involved also actively participates. The local community will play the most important role here. The answer to how to solve such a problem is in social entrepreneurship, which will certainly connect and effectively implement the development of self-sufficiency.

One of the extremely important aspects of social entrepreneurship is undoubtedly the participation of all actors in the local community. The local community is a platform where stakeholders who have recognized the social problem and are ready to solve it meet. The local community is all the inhabitants of individual areas and the development of the local community is our common responsibility.

Co-responsibility for the development of the community in which we live, responsibility for ourselves, our environment and resolving issues that arise in the local community is the first step for its development. The local community is the driving force behind the development of social entrepreneurship, as it provides challenges as well as answers and opportunities for the development of entrepreneurial ideas, and with its active role participates in solving basic and broader social problems. If we talk about the »leadership« of the local community, its role is to give ideas and challenges the opportunity, create conditions for their prosperity, provide a healthy environment for the development of ideas and the implementation of good solutions in life. Practice has shown us, unfortunately too rarely, that all administrative barriers are surmountable if there are people on both banks who are willing to engage in dialogue and co-operation. The local community is the first to be called upon to be ready to create an environment in which a positive entrepreneurial climate based on the principles of social entrepreneurship is spreading. Social entrepreneurship is also a great example of good CSR practice.

7. Corporate Social Responsibility and Vulnerable Groups

Without respect for the dignity of fellow human beings, we cannot imagine a welfare society and a welfare state. Such a label deserves only a society in which caring for a fellow human being is among its fundamental guidelines. Concern for one's fellow man is in one way or another related to all other value domains, especially, of course, humanity, culture, universalism and respect for life, health, nature and the environment. Without an emphasis on caring for one's fellow man, it is difficult to imagine wisdom and knowledge, justice and integrity, as well as good tradition and creativity. It is a principle that can be connected with the essence of humanity, and at the same time connects humanity with other value domains, especially by caring for fellow human beings. Justice, it seems, is one of the fundamental guidelines of man, of the social being in coexistence with other people, and of the individual in relation to the cosmos.

The moral task of individuals (»professionals«) is not to promote more or less equality, but to become an ethical principle of a democratic society. Recognizing people means treating them equally, with respect and consideration, it also means requiring them to be guaranteed freedom and the rights necessary to protect that freedom when we place recognition as the paradigm of the problem of freedom and equality. Justice means belief and conduct that treats all people without exception and unconditionally equally, especially in sanctioning their actions.[20]

In particular, justice means equal protection and protection of individuals and groups, and equal respect for their rights without any bias or discrimination. Therefore, justice is one of the fundamental concepts of ethics, morality, law and is undoubtedly the main guideline of the rule of law and the rule of law. Before Aristotle, Plato, Aristotle's teacher, had already emphasized that justice is the most important virtue of an orderly society. Equal rights for all and equality before the law are fundamental features of the rule of law and signify the realization of universal equality. A fair society is therefore a society in which there is no degrading inequality.[21] Impartiality exists in this understanding of the commandment not to treat any person differently.[22]

In Slovenia, Article 14 of the Constitution states that all citizens are guaranteed equal human rights and fundamental freedoms regardless of nationality, gender, race, language, religion, political or other beliefs, financial status, birth, education, social status, disability. or any other circumstance. Disability is seen as a human right and not a disease, as we still often and in public treat it in public. People with disabilities are not patients, but equal citizens. The European Union has guidelines in its founding acts, many initiatives and activities that promote the equal treatment of people with disabilities. The European Union is also combating discrimination through concrete action. One of the major actions was 2007, the Year of Equal Opportunities for All, in which a series of projects took place, the main aim of which was to raise the awareness of European citizens about the importance of anti-discrimination measures.

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20 Masterson, v: Ahern, Nutti, Masterson, 2000.

21 Margalit, 2002, page108.

22 Ritsert, 1997, page 13.

Among the documents that reiterate and ensure concern for the equality of European citizens is certainly the Lisbon Treaty, ratified by Slovenia in January 2008. Documents adopted at the global, European or national level are only a positive stimulus and a direction in which we are moving. of the future. With them, we pursue respect for human rights, the promotion of individual dignity and independence, respect for diversity and disability, and promote equal access to all information and communication. Too often, there is still a deep gap between the achievement of written goals and their realization in everyday life. The long-ignored social group of people with disabilities has long sought a fair placement in modern society. Many things are changing for the better, but there are still shortcomings that still need to be addressed. One of the fundamental aspects of integration is economic integration, which is later associated with psychological well-being and social integration. It is therefore crucial that we create the conditions for the integration of this population into the labour market. So we could talk about integration and inclusion, where inclusion implies a higher degree of environmental adaptation than integration. In what follows, we will use the term »inclusion« to mean both integration and inclusion. Economic integration is not just about achieving material well-being and therefore people being able to live comfortably, but about achieving integrity and a meaningful, value-linked life that is important for identity development.

Employment of vulnerable groups is an aspect of CSR that actively responds to the needs of the local community and can and must be placed in the field of self-sufficiency. People who live in the local community and have reduced working abilities and are not able to enter the labour market independently and equally must be offered the opportunity to perform work suitable for them within their abilities and thus ensure their own material independence. Material independence is a condition for equal inclusion in life and their contribution to the development of the local community. Every local community has the opportunity to offer these people employment opportunities in different areas of work. It is important that they are paid fairly for their honest work. In Slovenia, we have more opportunities to employ vulnerable groups and the task of social entrepreneurship in cooperation with the local community is to take advantage of these opportunities. We would like to emphasize that the positive aspects of employment for people with disabilities are seen in several segments that are intertwined. The form of employment in one's own, local environment is of special importance, as it offers people security, mobility from home to work and, last but not least, employment in jobs they are used to and for which they are at least partially qualified. The right to work and employment is a fundamental human right. As soon as we start from this fact, we find that creating an environment that allows the exercise of this right is crucial for the development of the individual. Everyone, including people with disabilities and people with special needs, wants their co-workers and the environment in which we work to be positive and stimulating, and for mutual respect to prevail. Adjustments to the workplace and work environment for people with disabilities, which according to the WHO represent 10% of the world's population and are growing in number, are suddenly becoming adjustments for people with disabilities special needs. We start from the premise that we humans are beings who want and want to work. There are few who do not feel this need. Satisfaction, happiness and empowerment come from work, as well as payment for work done. The latter enables economic integration, which in our opinion is the foundation of any integration. We understand these starting points as valid for all people who have preserved any ability to work. Accordingly, the professional careers of people with disabilities should also be planned and taken care of. All too often, the field of work and careers is reserved only for people whose working capacity is not assessed as reduced. A working career is a sequence of work positions that an individual performs in his / her work or employment period. Career also has subjective aspects. It is not just a technical concept that helps us logically organize a multitude of works, but a perspective from which a person interprets holistically what happens to him at work and to which an individual's personal aspirations, values, emotions and self-concept are tied. Unemployment, especially if it lasts for a long time, on the other hand, carries many risks for psychological, physical and any kind of well-being. The key role in this is employment. They could test their abilities, but because they did not have the opportunity to test and prove themselves, they remained passive. This is also the case if people are assigned an annuity under the label of being »incapable«, otherwise it allows for passivation and marginalization.

8. Conclusion

Only active integration into society gives a sense of integrity and a personal sense of competence, which is the foundation of a healthy and satisfied personality. Central to mental health is a sense of human dignity and justice, linked to health, well-being and successful coping with the demands of life. Identity is created through lifelong interactions with fellow human beings, the environment and society. What matters is how other people see us, which we eventually take over and internalize. It takes positive responses from other people to be able to learn to value themselves. The lack of positive responses, however, leads to poor self-esteem and leads to the development of a damaged identity. They do not achieve the same high results in life as people who have higher working abilities, and as a result they do not receive a certificate for the work they do. In fact, due to reduced capabilities, they did not have the opportunity to have the same achievements as most at the outset. So we can say that capabilities come from possibilities. These are risks that we know in advance. These are the risk of being pushed to the margins of society, the risk of personal injury to themselves and their families, the risk of lower socio-economic status, poverty, etc. In society, these people and their families are often »less valuable«, marked, ridiculed and victims of various prejudices and ignorance. The development of identity, favourable self-image and empowerment in people who do not have the opportunity to work but are able to work is thus threatened. Let us add at this point that, in accordance with the above, all those who are able to work should also have the opportunity for regular employment. Risk of low socio-economic situation, poverty, deprivation, poor health care, weak social networks, etc. there is a lot for the unemployed. Unemployed people are often passive, isolated and hopeless, with many of the consequences that this brings; e.g. depression, ill health, poverty. Such a situation poses a serious danger to society, not only in terms of violating the provision that Slovenia is a welfare state, but also the refusal to increase social danger and exclusion. That is why CSR is all the more important, as it involves all people in work, instead of excluding them and making them passive.

By doing so, it brings freshness to society and the hope that things can move for the better, that social prosperity for all can truly come to life. This is a great opportunity for CSR to become the standard in our business environment. It is about the interconnectedness / dependence between efficiency as social responsibility. In the future, only socially responsible companies will be successful and vice versa. Society must make a holistic effort to ensure that all work is able to be included in the work, as this brings to the fore all the creative potential that society can offer. With CSR, society is becoming more efficient in the whole sense, also in terms of added value and its economic efficiency. The more the active population works, the greater the inflow of taxes and the higher is the level of social security of the population. CSR paves the way for the effectiveness of corporate governance and vice versa. Only an economy based on CSR can make a constructive contribution to social well-being, as it ensures a higher social level of social rights - from good health, infrastructure, security…, all of which significantly affect the quality of life of the individual.

We often say that every human being is precious. So what is the price of priceless values?

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PRINCIPLES OF CORPORATE GOVERNANCE IN THE LIGHT OF CRISES AND EU DIRECTIVES

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Abstract

Banks and financial organisations are playing a key role in the continual recovery from the consequences of the crisis, including by influencing the development of corporate governance. The legal provisions are binding on all participants in the market, and sanctions are expected in the event of a breach, which, consequently, allows the investor some legal certainty.

Centralised systems are usually coordination systems, while decentralised systems are usually protective systems. Which system prevails depends on the existence and character of the institution, and on the courts, lawyers, law enforcement agencies, trade unions and business groups.

It is important to be aware that the biggest differences in the practice of implementing corporate governance do not stem from the recommendations of the Corporate Governance Codes, but from different corporate and securities law regimes.

Key words: transparency, effective legal framework, effective regulatory framework, corporate governance, guidelines.

1. Introduction

1.1 Definition of the area and description of the problem

The importance of good corporate governance has come to the fore in the wake of the economic and financial crisis that began in 2007, when it emerged that corporate governance was not working as expected, and that shortcomings and weaknesses in corporate governance were, to some extent, also reflected in the scale of the economic and financial crisis. Adams and Mehran (2008) say that mismanagement played an important role in the mortgage crisis.

Information on risk exposure in certain cases was not provided to the boards of Directors or even top management, risk management was often dealt with in the short term rather than the long term, and the method of remuneration also encouraged short-term thinking (Kirkpatrick, 2009). The method of remuneration, with its short-term orientation and structure of rewards, led to extreme risks, which were short-term oriented and did not take into account the long-term nature of the risks, nor did the policy of rewards foresee penalties for mistakes made.

Banks and financial organisations are playing a key role in the continual recovery from the consequences of the crisis, including by influencing the development of corporate governance in other companies through their own operations. As it turns out, shortcomings in banking corporate governance can destabilise the entire financial system and create systemic risk in the economy. As Caprio and Levine say, corporate governance of banks (2002) is important for banks, as well as for the economy as a whole. Moreover, corporate governance of banks is crucial for growth and development (Levine, 2004). In the most recent financial crisis, management tools were identified as ineffective when faced with unexpected pressures and significant conflicts of interest. Banks are, therefore, now in a position to influence the corporate governance of their borrowing clients. As such, they must take care of themselves and ensure good corporate governance at the outset.

Differences between banks and other companies are also reflected in differences in the way they are managed. Banks have a much larger number of clients with whom they have a stake in their activities compared to other companies, and that makes it difficult to manage them. Stakeholders in banks include, in addition to shareholders, depositaries, investors, the state and other creditors. Despite the fact that board members have the same legal responsibilities, additional expectations apply to the board of Directors in banks. These are usually laid out in laws and recommendations that reflect the expectations of safe and secure financial institutions. The presence of legislation should lead to the creation of internal governance mechanisms. One of the more important areas in terms of legislation is the method of reward. Appropriate legislation will also take risks into account. Thus, for example, remuneration in the form of stock options is acceptable for a company, however, this method of remuneration in banks can be controversial, since protecting depositors and taxpayers must also be a focus of the business.

Given the fact that banks have played a key role in the recent financial crisis, and given that their role will also be very important for getting out of the crisis, it is very important for banks to have good corporate governance. This affects the performance of their business, while corporate governance of banks is reflected in other companies as well, and, consequently, the entire economy.

1.1.1 Corporate governance

Corporate governance covers many different areas (law, economics, ethics, politics, management, finance, etc.), the consequences of which are reflected in the various definitions of this concept.

If the underlying reasons for such a trend are the same, there nevertheless exist differences in the socio-economic environment. In addition to the ownership structure, political, cultural and other factors contribute to the establishment of different corporate governance systems, as well as the relationship between the functioning and the management of the company. In the transition economies of Central Europe, predominantly concentrated ownership enables top management to wield excessive power and to pay insufficient attention to the company's shareholders. That is to say, the absence of a strong legal mechanism that would effectively protect the rights of minority shareholders increases the influence top management has. Also, such an ownership structure does not guarantee the inflow of fresh capital into companies.

According to Bohinc and Bratina, the concept of corporate governance (2005, p. 46) dates back to 1932, when, in the USA, the work of authors Berle and Means was created, entitled *Modern Corporation and Private Property*. In this work, Berle and Means concluded that the owners of large companies do not manage themselves, but leave the management to external experts. Berle (Bohinc & Bratina, 2005, p. 46) and Means also noted that there is a separation between the ownership and control of these companies, and, consequently, the question arises as to how the owner (principal) can ensure that their company, which is run by managers (agents), will really be run in their interest and for their benefit. The relationship between the principal and the agent, which, in fact, constitutes the central problem addressed by corporate governance, is referred to in the literature as the principal-agent problem.

The principal-agent problem arises when managers entrusted by the owners (i.e. shareholders) with the role of managing the company, manage the company in such a way as to follow their own interests (i.e. short-term successes of the company's operations) and not the interests of the company's owners. In order to eliminate or minimise the principal-agent problem and improve shareholder control over the work of managers, it is necessary to establish appropriate mechanisms in such a way that the expectations of the owners are met, and that the business activities of managers is in their interests. So, in addition to generating profits, economic operators must also satisfy the interests of shareholders (dividends, increase in the value of the company), creditors (payment of receivables), workers (appropriate payment, reliable and permanent employment), consumers (quality products and services), public (state) interests (payment of taxes, contributions, donations, etc.) and environmental protection interests (treatment plants, newer and cleaner technologies, etc.) (Bohinc & Bratina, 2005, p. 130). As Allen and Carletti noted, (2010, p. 51) the agency problem in Japan and Germany, due to the lack of a strong market for corporate supervision, is resolved through banks acting as external supervisors/observers. A feature of this relationship is the creation of a close and long-term relationship between the bank and the company, based on the fact that the bank grants the company a loan and owns the company's shares. The role of the bank becomes important mainly in times of financial crises, while its role is less important when the company is doing well.

1.2 Corporate governance in times of crisis

> *The failure to anticipate the timing, scale and severity of this crisis and to resolve it was, above all, the failure of the collective imagination of many smart people, both in this country and internationally, to understand the risks of the system as a whole.* (British Academy Forum, 2009)

According to Reed (2002, p. 231), changes in corporate governance systems in developing countries are taking place in response to structural change in the international economy and not entirely successful interventionist development models. The main rationale for economic liberalisation and deregulation is that the impact on development will be greater than that of previous interventionist programmes. The main sources of development impact were private corporations, which were considered »primary drivers of development«. The adoption of an Anglo-American corporate governance model was understood to be the main element promoting the »development potential« of corporations. Poor governance contributed heavily to the global financial crisis. Better governance in the financial sector would have prevented the financial crisis and certainly reduced its impact (Mayes & Wood, 2013).

Financial supervision did not address the stability issues of the financial system as a whole. Their work focused on the strength and stability of each individual institution within the whole sector. The exception was the Financial Services Authority (hereinafter FSA) from the UK, which prepared an annual risk review and proposed scenarios for the operations of the financial sector. As a result, no one was clearly responsible for the situation in most countries (Mayes & Wood, 2013).

Sheppard (2013, p. 32) states that three errors were made in the system: (i) The legal framework was inadequate for the protection of the rights of small shareholders, creditors, and even clients, (ii) The regulatory framework, which involved several regulators with limited influence, resulted in bad behaviour, and this behaviour was not penalised, and (iii) The shareholders were not successful in exercising the rights they had. By reviewing and exercising their power carefully, they could do much to improve the company's operations. According to Sheppard, (2013, p. 34) the components of a fiasco of financial companies in times of crisis are:

- Greed and stupidity (of investors and financial companies),
- Uncoordinated incentives,
- Failure of management,
- Regulatory failure.

If there is one lesson to be taken from the recent financial crisis, it is that corporate governance is important. The central irony of governance failures in this crisis is that many of them have occurred in some of the most sophisticated banks, operating in some of the most developed governance environments in the world (Ard & Berg, 2010). Sun and others (2011, p. 17) believe that the failure of the corporate governance system refers to the failure of regulatory management, market management, stakeholder management and internal (or shareholder) management.

The German model attaches less importance to the financial markets, and was less affected during the financial crisis (Pérez, 2011, p. 123). As Pérez says, it may be useful for this system to be adopted throughout Europe. This would mean abandoning the »French style« of management structure with its Management Board and Chief Executive Officer, and introducing a two-tier »German style« management with its supervisory board and administration. (Pérez, 2011, p. 125) As part of the new governance framework, Pérez also refers to a corporate governance system that is less focused on shareholders and more on stakeholders. The vision of governance should be broader and more accountable.

Nicolaescu (2012) analyses the impact of corporate governance mechanisms on company operations and the relationship between company operations and corporate governance in times of crisis. The operation of Chinese financial companies has not improved through the use of corporate governance. Companies with several independent members in its supervisory board and greater institutional ownership performed worse in times of crisis, because, in such times, independent members of a supervisory board are associated with capital increases. While there is supervisory board independence, the incentivised remuneration and separation of functions of the CEO and the Chairman of the management board (supervisory board) have proven to be detrimental to the business of companies in times of crisis.

Villiers (2010, p. 287) argues that institutional investors have played an important role in the recent financial crisis and, in the future, proposes to (Villiers, 2010, p. 300) improve the efficiency of shareholder engagement through the following measures: (i) Improving transparency, which may require regulatory changes; (ii) Improving the participation of institutional investors (they may be more effective collectively than if acting individually) and the enforcement of their rights, including the removal of members of the supervisory board; (iii) There should be mandatory disclosure requirements for shareholder voting and reports on engagement with clients and other shareholders; (iv) Establishing a clear relationship between Corporate Social Responsibility and corporate governance strategies that identify those relationships and their impacts on one another clearly; and (v) More resources are needed to monitor and carry out business activities effectively, and shift the culture of business from short-term challenges and issues to long-term ones. Compliance with these measures for ongoing and major changes is not enough. Structural changes are also needed in the areas of economic, law and corporate culture. A radical step would be to limit or eradicate the concept of limited liability, forcing shareholders to work more closely with the supervisory board and to be more willing to intervene in the activities of their corporation.

1.3 Legal frameworks in the field of Corporate Governance

The laws adopted in individual countries form the basis of company law, and are in force at the national level, with the legislation adopted at a European level. At the European level, the Directives adopted obliged member states to adapt their legislation, in particular in the following areas (Bohinc & Bratina, 2005, p. 61): (i) Public disclosure of information and publications (legal and financial status of companies), (ii) Ensuring the protection of third parties with whom the company enters into contact, (iii) Voiding of the company, (iv) Capital issues (e.g. establishment and operation of a public limited liability company), (v) Mergers/divisions of public limited liability companies, (vi) The composition, adoption and publication of accounts and/or the consolidated Balance Sheet, and (vii) Unification of publication requirements in relation to branches. Meanwhile, internal relationships within companies are mostly regulated by Statutes, Articles of Association and other Acts that the company has. According to Bohinc and Bratina, good business practices and autonomous legal sources (2005, p. 38) are also an important legal source.

The legal provisions are binding on all participants in the market, and sanctions are expected in the event of a breach, which, consequently, allows the investor some legal certainty. An autonomous legal source (e.g. a code) is considered not to be binding, and non-compliance with it does not lead to legal sanctions. Operations in accordance with codes/proposals/recommendations/guidelines are, therefore, not mandatory by law, but companies are increasingly expected to comply with them. Therefore, especially for companies, if they fail to comply with any of the recommendations, they must disclose this. Failure to comply with the rules of the autonomous legal source has certain consequences. As stated by Bratina and Pašić (2010), investors first react to inconsistent behaviour, and their reaction is reflected directly in the securities market. The advantage of an autonomous legal source over legal provisions lies in fewer formalities at the time of adoption, and in a much more rapid and flexible response to market needs. Autonomous legal sources have been developed and created on a country-by-country basis, where they have been prepared and issued by various institutions (e.g. associations, exchanges, institutes, institutional investors, companies, etc.), with the support of governments and international organisations. One of the most influential autonomous legal sources is the set of OECD principles and guidelines, which are often used by countries as a basis in the preparation and implementation of their guidelines.

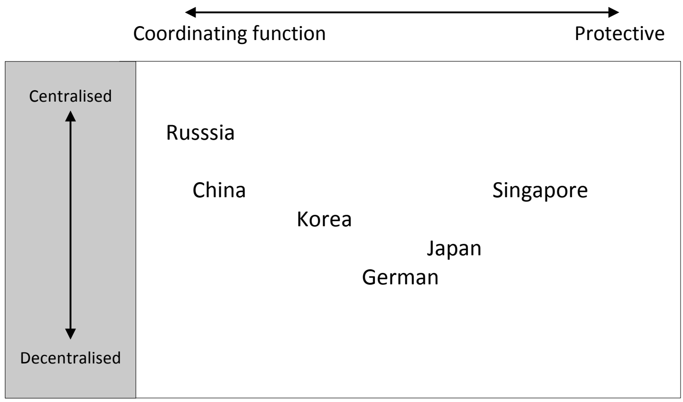
To understand the differences between the various legal systems around the world, it is useful to know how they differ in just two dimensions: Centralised/decentralised, and coordinated/protected (Milhaupt & Pistor, 2008, p. 182). Milhaupt and Pistor (2008, pp. 194-195), with the help of a formulated analytical framework, examined some legal systems around the world. The results of the comparative analysis show two:

1. Legal systems can be classified according to two important dimensions, namely: (i) The organisation and (ii) The main tasks they perform. This classification has an affinity for the traditional division into the civil law vs. common-law system, and this analytical framework is more appropriate for taking into account changes over time within and between systems;
2. Each system has its own costs, benefits and system-related disadvantages, which can lead to a crisis, and, in extreme cases, to the collapse of the system.

Milhaupt and Pistor (2008, pp. 182-183) created a matrix showing the typology of legal governance.

Figure 1 shows the legal systems of seven countries, which have been analysed in more detail by the two authors.

Figure 1: Matrix of legal systems



Source: Milhaupt and Pistor (2008, p. 183)

The matrix is for illustrative purposes, where the position of an individual country relative to another is important. The axis of abscissas shows the task/function of the law. The law can perform several functions in support of market-oriented economic activity. As stated by Milhaupt and Pistor (2008, pp. 6-7), the clear assignment and protection of ownership rights is one of the functions of the law. In some jurisdictions, this protective function is dominant. In other systems, the remaining control rights are allocated to several agents, who, within statutory limits, are encouraged or even forced to barter over the outcome. These systems are dominated by the coordinating function. Centralised systems are usually coordination systems, while decentralised systems are usually protective systems. Which system prevails depends on the existence and character of the institution, and on the courts, lawyers, law enforcement agencies, trade unions and business groups. After the introduction of one system, it is, subsequently, extremely difficult to change it. Milhaupt and Pistor (2008, p. 176) state that the degree of centralisation is determined by the number and identity of social actors involved in the creation and enforcement of the law. The more actors there are in the system, the more decentralised it is. They emphasise that it is not always appropriate to link higher levels of state control with greater centralisation (Milhaupt & Pistor, 2008, p. 178). As they say, political organisation is an important predictor of the organisation of the legal and economic systems.

Regulators will always have to adopt new approaches in response to market conditions. Regulations can have an impact on more efficient operations, but they can also lead to costs. The direct impact of legislation can be reflected in a reduction in output and consumption, while reducing risks in the economy, on the other hand, has a positive impact, and can more than compensate for costs (Barrell, Hurst, & Kirby, 2010, p. 66).

Below we present in more detail the OECD Principles of Corporate Governance, OECD Guidelines for the Corporate Governance of State-Owned Companies, European Corporate Governance Guidelines for Unlisted Companies, Corporate Governance Codes, Good Practice Guidelines in Corporate Governance Disclosures and Standards in the Field of Financial and Financial Reporting and Auditing, which also represent the substantive basis of Corporate Governance for the countries of Central and Eastern Europe that are the subject of this Doctoral Dissertation.

1.3.1 G20/OECD Corporate Governance principles

The first OECD Principles of Corporate Governance were adopted in 1999. In 2004 the Principles were revised for the first time, as a result of the achievements and experience of the member states and non-OECD countries. In 2014, the OECD began a revision of the 2004 principles and published a new version of the principles in 2015, this time called the G20/OECD Principles of Corporate Governance. Cooperation with the G20 gives the principles global reach, and involves the experience and ambitions of different countries at different stages of development and with different legal systems. The principles identify key building blocks for a good corporate governance framework, and provide practical guidance for implementation at the national level. The principles include new insights of corporate governance out of the global financial crisis, increased cross-border ownership, changes in the functioning of Stock Markets and the consequences of longer and more complex investment flows from household savings to corporate investment (Organisation for Economic Co-operation and Development, 2015, p. 7). The principles aim to (i) Be concise, understandable and accessible to the international community, and (ii) Assist policy makers in assessing and improving the legal, regulatory and institutional framework for corporate governance, in order to support economic efficiency, sustainable growth and financial stability in the country, which can be achieved by providing the right incentives for shareholders, board members, managers, financial intermediaries and service providers to perform their duties. The principles may apply to public (financial and non-financial) limited liability companies, as well as to non-limited liability companies, notwithstanding the fact that some principles may be fundamentally more appropriate for larger companies. The principles are non-binding and do not aim to lay down detailed rules for national legislation, but seek to define objectives and propose different means of achieving them. The principles aim to create robust, but flexible frameworks, for policy makers and market participants to develop their own corporate governance frameworks that provide them with sufficient flexibility to operate effectively in a competitive and changing environment (Organisation for Economic Co-operation and Development, 2015, pp. 9-11).

The principles are presented in six chapters (Organisation for Economic Co-operation and Development, 2015, p. 11), namely:

1. Provision of a basis for an effective corporate governance framework;
2. Rights and equal treatment of shareholders and key ownership functions;
3. Institutional investors, stock markets and other intermediaries;
4. Role of stakeholders;
5. Publication of data and transparency;
6. Responsibilities of the board.

Each principle is followed by a corresponding sub-principle. The principles are supplemented by interpretations and explanations intended to help understand the purpose of the principles. They may also include descriptions of prevailing or emerging trends and offer alternative implementation methods, as well as examples that may be useful in putting the principles into operation.

According to the OECD (Organisation for Economic Co-operation and Development, 2015, p. 11) the principles are evolutionary in nature, and are reviewed in the event of significant changes in circumstances in order to maintain their role as the leading instrument for policy-making in the field of Corporate Governance.

As stated in the OECD Principles (Organisation for Economic Co-operation and Development, 2015, p. 10), corporate governance policies play an important role in achieving broader economic objectives in relation to investor confidence, creating capital, and their allocation. The quality of corporate governance affects the company's costs of accessing capital for growth, and the confidence with which those providing capital – directly or indirectly – can participate in value creation on fair and equitable terms. Good corporate governance helps protect the rights of shareholders and other stakeholders, reduce capital costs and facilitates access to the capital market.

1.3.2 OECD Guidelines for the Corporate Governance of State-Owned Enterprises

Picou and Rubach (2006) define corporate governance guidelines as a mechanism which a company can enact, and which should reduce the costs of representation (i.e. agency costs), and establish a better relationship between the interests of management and capital providers. The results of a survey carried out on a sample of 77 companies show that good governance is important. Companies that have announced that they have adopted corporate governance guidelines have witnessed a rise in share prices. Companies that published all or part of the content from the field of Corporate Governance Guidelines witnessed an immediate reaction (1-4 daily response). Companies that merely announced that they were following the Guidelines received a slower reaction (8-10 days).

The OECD Guidelines for the Corporate Governance of State-Owned Enterprises (hereinafter referred to as the OECD Guidelines) refer explicitly to the governance of state-owned enterprises, and are complementary to and in full agreement with the Principles. The basic purpose of the Guidelines is to provide general advice to governments on improving the operations of state-owned enterprises, effective management and the application of good management practices to state-owned enterprises. Compliance with the Guidelines does not bring about the non-acceptance of the country's programmes and privatisation policies. The Guidelines are divided into two parts. The first part includes six Guidelines and their descriptions, while the second part provides notes and more detailed explanations of individual Guidelines:

I. Ensuring an effective legal and regulatory framework for state-owned enterprises: It must, among other things, ensure a level playing field between state-owned enterprises and privately owned companies; a clear dividing line must be drawn between the state's ownership function and other government functions (i.e. the function of the state as the market regulator); the operational procedures and legal form of state-owned enterprises must be simplified and unified; the obligations and tasks to be performed by the state-owned enterprise in relation to public services must be delegated clearly; the capital structures of state-owned enterprises must be adapted to meet the objectives of the company, but the mechanisms used must be supervised and documented properly in order to avoid their exploitation; etc.

II. The state in the role of owner: It must act as an active and informed owner; it is obliged to adopt a clear and consistent ownership policy; the government must not interfere in the day-to-day management of state-owned companies, and must leave the performance of tasks to the boards of companies and allow them full independence in operations; the ownership function of the state should be centralised for the pursuance of ownership rights; the ownership body must be accountable to representative bodies (e.g. parliament), and must have a clear relationship with relevant public bodies, such as the supreme state audit institutions.

III. Impartial treatment of shareholders: State-owned companies are obliged to ensure impartial treatment of all shareholders; recognise shareholder rights; grant shareholders equal access to corporate information; encourage minority shareholders to participate in shareholder meetings.

IV. Relationships with stakeholders (i.e. with the company's stakeholders, e.g. employees, shareholders, banks): State-owned enterprises must be accountable to their stakeholders; they must report on their relationships with stakeholders in order to establish reputation and transparency; they must establish mechanisms and procedures to protect stakeholder rights; they must operate in accordance with high ethical standards and internal codes of ethics.

V. Transparency and publication of data: State-owned enterprises are obliged to develop Summary Reports on all state-owned enterprises;

they are obliged to publish a Summary Report on their operations every year, which is intended for the general public, parliament and the media; they are obliged to introduce effective internal audit procedures and functions; their operations must be checked annually by an independent external auditor, in addition to specific state audits, according to international standards, and they must not offer advisory and non-audit services, while there must be a periodic switch of audit firms and associates; they are obliged to publish data on their operations in a transparent manner and in accordance with internationally recognised Standards.

VI. The tasks of state-owned enterprise boards: The boards must have powers and competences, and exercise strategic leadership and control over management impartially; they must act honestly, responsibly and qualitatively; they must be given a clear mandate and the highest responsibility for the operations of the company; they must act in the interest of the company and treat all shareholders impartially; their responsibility and the personal responsibility of board members must be defined properly in the legislation, Regulations, etc.; in order to achieve greater efficiency, boards should apply the principles of good practice stemming from the private sector, and reduce the size of the board (better debates, less bureaucratic); prepare a Management Report, which must be an integral part of the Annual Report, and, thus, also part of the review of the external auditors; the holder with the power to appoint and dismiss the Chief Executive Officer, as only in this way can they feel responsible for the company's operations and perform their supervisory function fully; influence the remuneration of the Chief Executive Officer, which must be tied to business results and duly published; composition, which allows them to issue objective and independent opinions based on the separation of the functions of the Chairman and Chief Executive Officer (valid for a unified system), or incompatibility of the function of the President of the Management Board and the President of the Supervisory Board (two-tier management system; applies mainly to Slovenia). Where there are representatives of employees on the board, it is necessary to ensure that they have the same functions and responsibilities as other members of the board, and represent the interests of the company and the shareholders. If necessary, company boards should establish special committees (e.g. an Audit Committee, Remuneration Committee, Strategic Committee, Ethics Committee, Risk Management Committee and a Purchasing Committee) to support their work, and which are aimed primarily at strengthening the work of company boards and supporting their key responsibilities; they are obliged to carry out an annual assessment of their work, which is aimed at determining the competence of board members and achieving even greater professional competence of the state-owned enterprise board.

1.3.3 European Corporate Governance Guidelines for Unlisted Companies

On 24 March 2010, the European Confederation of Associations of Members of Boards of Directors and Supervisory Boards (hereinafter ECODA) presented to the European Parliament the Corporate Governance Guidance and Principles for Unlisted Companies in Europe, the main purpose of which is to make recommendations for achieving the efficient functioning of Boards of Directors and Supervisory Boards and the transparent operation of unlisted companies.

The document consists of fourteen Guidelines for good governance, which take into account the degree of openness, size, complexity and level of development of each company, with the first nine Guidelines referring to all unlisted companies, while the remaining Guidelines refer to larger and/or more complex unlisted companies (Table 1):

Table 1: European Corporate Governance Guidelines for Non-Public Companies

Guideline No.	Guideline description
Guideline No. 1	Shareholders should establish an appropriate statutory and management framework for the company
Guideline No. 2	Each company should endeavour to establish an effective board of Directors/supervisory board responsible for the long-term success of the company, including defining the corporate strategy. An intermediate step towards the establishment of an effective (and independent) board of directors/supervisory board may be the establishment of an advisory board.
Guideline No. 3	The size and composition of the board of Directors/supervisory board should reflect the scope and complexity of the company's activities.

Guideline No. 4	The board of Directors/supervisory board should meet frequently enough to carry out its responsibilities and be provided with the necessary information in a timely manner.
Guideline No. 5	Remuneration should be appropriate to attract, retain and motivate the members of the board of Directors/ supervisory board to perform their work well.
Guideline No. 6	The board of Directors/supervisory board is responsible for the control of risk, and should establish an appropriate system of internal controls to protect shareholder investments and the company's assets.
Guideline No. 7	There should be dialogue between the board of Directors/ supervisory board and the shareholders. The board of directors/supervisory board should not forget that all shareholders must be treated equally.
Guideline No. 8	All Directors/members should be introduced to the work of the board of Directors/supervisory board and should receive ongoing training.
Guideline No. 9	Family businesses should establish governance mechanisms that promote coordination and mutual understanding between family members, as well as the building of a relationship between family governance and corporate governance.
Guideline No. 10	There should be clear delimiting of the responsibilities of the company's management between the work of the board of Directors/supervisory board and the management of the company's operations. No one person should have unconditional decision-making power.
Guideline No. 11	The structure of the board of Directors/supervisory board varies according to legislative provisions and corporate norms. However, all boards of Directors/supervisory boards should be composed of Directors/members with sufficient competence and experience. No individual (or small group of individuals) should dominate the decision-making process of the board of Directors/supervisory board.
Guideline No. 12	The board of Directors/supervisory board should establish an appropriate committee to more effectively discharge responsibilities.
Guideline No. 13	The board of Directors/supervisory board should periodically evaluate its work and the work of individual Directors/members.
Guideline No. 14	The board of Directors/supervisory board should present a balanced and comprehensive assessment of the company's situation for all stakeholders of the company, and establish an appropriate stakeholder engagement program.

Source: Adapted from: Bratina and Pasic (2010) and European Corporate Governance Guidelines for Unlisted Companies (European Confederation of Directors' Associations, 2010).

1.3.4 Corporate Governance Codes

Corporate Governance Codes in the European Union recommend a one-track governance system in eight countries and a two-track governance system in ten countries. In the remaining nine countries, a so-called hybrid system is used, whereby companies can choose between a one-track and a two-track management system (European Commission, 2013).

The Code is an autonomous legal source whose non-compliance does not lead to legal sanctions, but non-compliance with its rules may nevertheless have certain consequences (e.g. investor response reflected in the securities market). Companies shall publish deviations from the provisions of the Code once a year in a Management Statement. In this way, the company informs its investors about the deviations from the principles of the Code and the reasons for them.

One of the more important advantages of the Code as an autonomous legal source compared to legal provisions is that it responds much more quickly and flexibly to market needs. Reviews and updates of Corporate Governance Codes are triggered by various factors, including the impact of the EU, the transition from soft law to legislative provisions, perception of good practices and market expectations, and lessons learned from compliance monitoring. The financial crisis, which has highlighted a number of problem areas, now acts as a catalyst for revisions to Corporate Governance Codes (Allen&Overy, 2012, p. 1).

Corporate Governance Codes are most often formulated and adopted by business, economic or academic associations, associations of directors and groups of investors (in Slovenia e.g. the Ljubljana Stock Exchange, the Association of Supervisors of Slovenia, and the Manager's Association), government institutions, committees or commissions formed by governments or Stock Exchanges, and international institutions (e.g. OECD – Principles of Corporate Governance). Consequently, the mechanisms and role of individual Codes may vary considerably. It is important to be aware that the biggest differences in the practice of implementing corporate governance do not stem from the recommendations of the Corporate Governance Codes, but from different corporate and securities law regimes. Smaller differences between Codes, and different numbers of Codes in individual countries, do not, however, constitute an obstacle to the functioning of an integrated European equity or capital market. On the way to the convergence of Corporate Governance Codes, the European Commission has, thus, only been developing legislative activities to harmonise the areas underlying corporate supervision (Djokić, 2011, p. 82). As stated by Djokić (2011, p. 80), individual countries of the European Union have several Corporate Governance Codes (e.g. the UK has eleven, Germany has three). Some Corporate Governance Codes regulate the relationships between the company's bodies, while others regulate the relationships with the company's various stakeholders.

Corporate governance practices, which are enshrined in the Corporate Governance Codes, have been developed on the basis of (Codes Comparative Study p.6: v (Djokić, 2011, p. 62)):

- Different legal arrangements of corporate governance in individual countries,
- Stock Exchange rules for the admission of securities to regulated markets,
- Different business rules and operating methods in national contexts,
- Different cultural values and socio-economic traditions.

The principles of Corporate Governance Codes across countries are similar and their relevance is increasing. That is to say, when investing in a company, potential investors decide on the basis of the financial results of the company's operations, as well as the corporate governance of the company. Due to the high degree of comparability of Codes across countries, the convergence of corporate governance practices could be discussed, with Codes being a mechanism for further convergence of corporate governance systems (Codes Comparative Study, p. 6-7: in (Djokić, 2011, p. 63)

Corporate Governance Codes are not legally binding. If the Codes were to be integrated into the European continental-civilian concept of legal sources, they could, by their very legal nature, constitute, to a certain extent, the customs[1] and business practices[2] that

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1 Organisational technical comparisons can be made with legal and regulatory norms, except that they are not adopted by a state body, but by a person or an association of persons governed by private law (Djokić, 2011, p. 64).

2 Slovenian legal theory defines customs, together with other legal Standards, as formal sources of law. Tradition is one of the social standards enshrined in

should apply in the field of CorporateGgovernance (Djokić, 2011, p. 64).

In addition to the elements that are typical of the customs and business practices, the legal nature of the Codes is determined by the fact that the provisions of the Codes also contain recommendations that, in substance, guide the implementation of corporate governance in practice. The legal nature of the provisions of the Codes is characterised in particular by the ethical and moral functioning of the entities (Djokić, 2011, p. 65).

Corporate Governance Codes across EU countries are similar. They all follow the practice of converging corporate governance practices. Differences in corporate governance practices between EU countries stem mainly from differences in national laws, and not from the best practice recommendations contained in the Codes, which, in principle, share the same objectives.

1.3.5 Innovations and proposals of the European Commission in the field of Corporate Governance

The European Commission's overarching objectives in the field of Corporate Governance are, in particular, to increase the transparency of business operations and shareholder engagement. In April 2014, the European Commission adopted a package of measures to improve the governance of 10,000 companies listed on European Stock Exchanges, which are intended to contribute to the competitiveness and long-term financial sustainability of these companies. The package of measures refers to the key actions identified in the communication on the long-term financing of the European economy IP/14/320, dated 27 March (European Commission, 2014a), and includes (i) A proposal to revise the existing shareholder rights Directive (Direktiva 2007/36/ES Evropskega parlamenta in Sveta z dne 11. julija 2007 o uveljavljanju določenih pravic delničarjev družb, ki kotirajo na borzi, 2007), which will encourage shareholders to be more involved in the operation of the companies they invest in, to require greater responsibility on the part of the company's management and to act in the longterm interests of the company,

the judicial rules. Tradition, like other social Standards, is not an independent formal source of law. The conditions of its incorporation into the judicial rules are laid down by law, the custom being a subsidiary source of law.

(ii) A recommendation on the quality of corporate governance reporting (the »comply or explain« principle), which advocates the development of guidelines to improve the overall management reporting of listed companies, and (iii) Proposals concerning the single-member company Directive, which will help to reduce costs/eliminate complex registration procedures for subsidiaries and facilitate the business activities and operation of companies abroad. According to the European Commission, the changes will be mainly the following (European Commission, 2014b):

- Institutional investors and Asset Managers will become more transparent about their investments and the investment policies of the companies in which they invest;
- Companies will disclose clear, comparable and comprehensive information on their remuneration policies and in their performance report, while shareholders will have a better chance of monitoring the remuneration of Directors;
- Companies will need to provide better and timely information on related party transactions, and minority shareholders will be better protected from improper transactions;
- Proxy advisors will be more transparent about the methodologies for preparing voting recommendations and how they manage potential conflicts of interest;
- The exercise of shareholder rights (e.g. voting rights), especially in cross-border situations, will be facilitated, and companies will be able to identify their shareholders;
- Companies should provide better explanations in the event of non-compliance with national Corporate Governance Codes by providing shareholders and investors with more useful information.

Certain benefits of these measures can be expected (European Commission, 2014b):

1. *Businesses:* Improved transparency will lead to better information and investor decisions, and encourage investors to engage more in the businesses in which they invest,
2. *Shareholders and investors:* They will have more and better information to make decisions and protect their interests, including full use of their rights as shareholders,
3. *Retail investors and final beneficiaries:* They will receive better information to optimise investment decisions and influence the management of their holdings.

As Michel Barnier (European Commission, 2014c), European Commissioner for the internal market and services, says in a press release, the main purpose of the proposals is to encourage greater participation by shareholders in companies, which is made possible with the right to proper supervision of company management, which must also include mandatory disclosure of remuneration.

1. Revision of the shareholder rights Directive

Revision of the existing Directive would address the shortcomings in corporate governance. These shortcomings concern both listed companies and administrations, shareholders, intermediaries and representative consultancy firms. On the basis of the proposals, shareholders would be able to exercise their rights more easily and to a greater extent, e.g. they would require greater accountability of the company's management, they would act in the long-term interests of the company, stricter transparency requirements for institutional investors and Asset Managers, easier identification of shareholders in order to facilitate the exercise of rights, especially in cross-border cases, greater transparency of representative consultancy firms, a pan-European obligation to disclose remuneration, whereby companies would have to disclose information on their remuneration policy and its implementation in practice (currently remuneration is not linked to business results sufficiently, which is reflected in the shortterm orientation of management), whereby the policy would have to disclose information on how it contributes to the longterm interests and sustainability of the company, and should contain the maximum allowed remuneration of managers, and the ratio between the average salary of employees and the salaries of managers.

2. Recommendation of the Commission on the quality of corporate governance reporting (the »comply or explain« principle)

In this area, the Commission is committed to developing Guidelines to improve the quality of management declarations published by companies. It is very important for companies and investors to obtain relevant information about the companies in which they wish to invest, or with which they do business.

3. Single-member companies Directive

Key innovations in this area relate to the standardisation of requirements for the establishment of single-member limited liability companies abroad. A unified procedure is proposed to make it easier for these companies to operate in the European Union, notably through lower costs of starting a business and doing business abroad. It is proposed that Member States introduce in their national laws a legal form of company called Societas Unius Personae (SUP), which will be subject to the same rules and keep the same acronym throughout the European Union, and which could be registered online. The required minimum capital of the company would be at least 1 EUR, or at least one unit of national currency in the Member State in cases where the Euro is not the national currency, and the draft Statute would be available in all European languages and would be valid throughout the European Union. A high level of creditor protection would be achieved by the obligation to submit a Solvency Statement before any profit is paid, and to pay the profit only if the SUP shows positive results in the Balance Sheet check, and the remaining assets are sufficient to cover the liabilities. A sole shareholder has the right to make decisions without convening a General Meeting. A sole shareholder may become a natural person, though this function may be assumed by a legal person only in cases where the laws of the Member State of registration so permit. The SUP may also be transformed into another national legal form, or terminated.

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REMUNERATION POLICY AS A TOOL FOT BETTER CORPORATE GOVERNANCE IN THE COMPANY

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Abstract

Remuneration policy is a well-known document in financial companies, which they are also obliged to publish in accordance with EU regulations and Commission recommendations (2004/913/EC). Directive (EU) 2017/828/EC (the so-called Shareholder Rights Directive - SRD II) newly regulated and encouraged long-term participation of shareholders in the formulation of remuneration policy and adequate reporting of remuneration, which also extends to the non-financial field. To further modernize corporate law, the European Commission has also adopted an action plan that intends to involve shareholders more actively in the corporate governance structure in order to contribute to the long-term sustainability of companies in the EU.

In the light of harmonization, this modernization was necessarily followed by the Slovenian legislator and at the beginning of 2021 the amended Companies Act (ZGD-1) was adopted, which implemented the remuneration policy and reporting on this policy in the Slovenian corporate system. Reporting or, in a broader sense, disclosure of remuneration policy has been added to the very concept and scope of the remuneration policy. This is part of the general policy of the company and therefore disclosure is important to internal as well as external stakeholders. As corporate law, and especially corporate governance, regulates the relations between the management body (management or supervisory board), the supervisory body (supervisory board or board of directors), shareholders and stakeholders of the company (other stakeholders), corporate institutions must be placed in tense relations of rights and obligations between the bodies in the company, in order to improve the corporate environment and thus corporate governance itself. Namely, corporate governance also determines the structure (organization) that supports the company's goals, the means to achieve them and the monitoring of results. The purpose of corporate governance is to help create the environment of trust, transparency and accountability needed to promote long-term investment, financial stability and business integrity, thus also supporting stronger growth and the development of a more inclusive community. In addition to the legislative framework, it is therefore necessary to improve and change autonomous legal sources (eg corporate governance codes).

corporate governance in companies and make suggestions for further improvement.

Key words: remuneration policy, reporting, harmonization, corporate governance, stakeholders, SRD II

1. Introduction

The constant changes and challenges of the economic situation in the world and in EU, dictate the constant improvement of rules in the economy and beyond to achieve maximum impact in terms of corporate governance of economic entities. Corporate law and autonomous legal sources impose competencies and obligations on the members of management and supervisory bodies, and on the other hand the responsibility of these bodies and their members in relation to capital investors (stakeholders) and stakeholders is relatively stricter. An important role in establishing an optimal relationship between management, supervisory bodies and capital investors (assembly) is therefore represented by corporate legislation, which tries to place various corporate institutions in a complex system of operation in a company - corporate governance. Corporate solutions are partly conditioned by adopted and amended EU legislation, and partly by autonomous sources and good corporate practice (i.e. soft law). Among the latest innovations, the remuneration policy and reporting on it in companies is regulated in more detail, but it was necessary to implement it from EU regulations into national company laws.

The article is based on compliance with the harmonization regulations of EU law and the amended provisions of Slovenian Companies Act (hereinafter: ZGD-1)[1], which is the parent law in Slovenia (the so-called »corporate constitution«) and regulates the management of companies and relations between individual bodies in the company. Also, in the systematics of legal bases, the so called »soft law«, ie autonomous sources such as the Slovenian Corporate

1 Companies Act (Official Gazette of the Republic of Slovenia, No. 65/09 - official consolidated text, 33/11, 91/11, 32/12, 57/12, 44/13 - US decision, 82/13, 55/15, 15/17, 22/19 - ZPosS, 158/20 - ZIntPK-C and 18/21).

Governance Code (hereinafter: Code)[2] (with envisaged changes) and all infra-cited recommendations and guidelines of the EU and individual institutions.

2. Legal framework

Remuneration policy is a already well-known document in financial companies, as the last financial crisis in 2008 exposed significant risks in remuneration and remuneration of directors in proportion to the drive to achieve company profits, which, according to some, led to moral hazard. this is supposed to (co) contribute to the financial crisis. As a result, the EU has very quickly approached regulating (limiting) the area of remuneration with two approaches; as recommendations (optional autonomous law) and mandatory harmonization law through EU directives. The EU Commission Recommendation of 14 December 2004 fostering an appropriate regime for the remuneration of directors of listed companies (2004/913/EC)[3] and Commission Recommendation of 15 February 2005 on the role of non-executive or supervisory directors of listed companies and on the committees of the (supervisory) board (2005/162/EC)[4] and Commission Recommendations complementing the supra-defined recommendations (2009/385/EC). In addition, the

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2 The Slovene Corporate Governance Code for Listed Companies was jointly drawn up and adopted by the Ljubljana Stock Exchange Inc., the Slovenian Directors' Association and the Managers' Association of Slovenia on 18 March 2004. They agreed to amend and supplement it on 14 December 2005, 5 February 2007 and 8 December 2009. The Code in its current wording was drawn up and adopted by the Ljubljana Stock Exchange Inc. and the Slovenian Directors' Association on 27 October 2016 (edited in January 2018). Due to changes in legislation, a recast is being prepared in 2022.

3 Commission Recommendation of 14 December 2004 on the promotion of an adequate remuneration system for directors of public companies (2004/913/EC).

4 Commission Recommendation of 15 February 2005 on the role of non-executive directors or members of the supervisory board of public companies and on committees of the board of directors or supervisory board (2005/385/EC).

remuneration policy is regulated by the European Commission's 2010[5] and 2011[6] Green Paper on the Corporate Governance of Financial Institutions and the stricter rules on the governance of financial institutions of 2011, proposed by the European Commission under CRD IV[7] (Kocbek, 2021: 1075).

Mandatory sources of remuneration policy in the EU include Directive (EU) 2017/828/EC on the promotion of long-term participation of shareholders[8] (hereinafter: Shareholder Rights Directive - SRD II), Which amended Directive (EU) 2007/36/EC (hereinafter: Shareholder Rights Directive – SRD I).[9] Otherwise, the SRD I did not directly regulate the remuneration policy itself in a broader sense, so it was completely replaced and supplemented in this area by the SRD II. In order to further modernize remuneration policy and corporate governance, the European Commission has also adopted an Action Plan,[10] which intends to involve shareholders more actively in the corporate governance structure. The main purpose is to contribute to the long-term sustainability of companies in the EU.

The remuneration policy in a broader sense thus includes the policy (delimitation) of payments to members of management and supervisory bodies, and part of the remuneration policy is also the report or, in a broader sense, the disclosure of the remuneration policy. This is part of the general policy of the company and therefore disclosure is important to internal as well as external stakeholders. (Massena Partners, 2017) The discussed SRD II had to be implemented

5 Green Paper - Corporate governance of financial institutions and remuneration policy {COM (2010) 285 final} {COM (2010) 286 final} {SEC (2010) 669}.

6 Green Paper - The EU corporate governance framework {COM (2011) 164 final}.

7 COM (2011) 453 final in COM (2011) 452 final.

8 Directive (EC) 2017/828 of the European Parliament and of the Council of 17 May 2017 amending Directive 2007/36/EC as regards the promotion of long-term participation by shareholders - Shareholders' Directive II.

9 Directive 2007/36/EC of the European Parliament and of the Council of 11 July 2007 on the exercise of certain rights of shareholders in listed companies – SRD I.

10 Action plan: European company law and corporate governance - a modern legal framework for better shareholder participation and sustainable companies. COM (2012) 740 final.

in state legislation within the specifics of each state regulation by 10 June 2019, but some Member States and Slovenia were late due to the known crisis situation. With the amendment to the ZGD-1 (ZGD-1K)[11], the Republic of Slovenia implemented the guidelines deriving from the SRD II, because the regulation under the »obsolete« ZGD-1 was insufficiently decided and not was in line with the newly adopted SRD II and other recommendations and guidelines.

Since it is the directors (members of management bodies) and members of supervisory bodies who contribute with their work to the long-term success of the company's operations, in addition to the regulation of remuneration itself, it was necessary to regulate and place this area within the legal position. Since the SRD II primarily refers to joint stock companies whose securities are traded on a regulated market (public joint stock companies), it was necessary to place the remuneration policy in the legal organizational form of a joint stock company, which has a pragmatically regulated choice of management system in Slovenia. The situation itself may vary depending on the management system chosen; single-track or double-track. In Slovenia, a dualistic model of management prevails, which is characterized by a coherent and institutional and personal separation of management and control functions, while in a one-tier system both functions are connected within the same body, board of directors and in the company's autonomy. As the remuneration policy is somehow immanent to the personnel body in the joint stock company, it was necessary to include in ZGD-1 the decision of the General Meeting on the remuneration policy in the spirit of non-interference with individual competences of the company bodies (and their interests). a tool for achieving the company's business performance.

3. Implementation of the remuneration policy

Remuneration policy covers all principles and decisions regarding salaries and / or remuneration. It is defined as part of personnel policy. Remuneration and remuneration of members of supervisory,

11 ZGD-1K – Novella ZGD-1; Official Gazette of the RS, no. 18/2021 of 9. 2. 2021.

operational and management bodies have a major impact on the performance and achievement of good results in companies. They can influence a greater willingness to make strategic decisions to achieve long-term goals in society. One of the central conflicts of interest in most companies is the conflict between the personal interests of shareholders and other stakeholders who are supposed to strive for long-term development and lasting success. The basic principle - failure should not be rewarded - leads to the fact that remuneration policy is one of the main instruments that lead managers to accept greater risks for society (Bratina, U., 2020).

The great financial crisis and the accompanying media scandals have identified the remuneration of executives as one of the main triggers for taking excess risk. Based on the experience and market failures of companies, regulations have been developed that contribute to a clear, simple and transparent process of rewarding management bodies and enable shareholders to actively participate in determining managerial remuneration (Tomić et al., 2018).

Due to the very rapid development of capital markets, the trend of tracking »directors'« salaries was the first to appear in the United States. Over the last 50 years, the ratio of a manager's salary to a worker's salary there has increased by an average of 380%. The most significant change, however, is in the last 30 years. The economic crises (especially in 2008), on the other hand, showed serious errors in the management remuneration system. The most frequently highlighted are the lack of transparency, the lack of period limitation and the inability to reimburse bonuses already paid. Namely, management decisions are often short-term oriented, motivated by accompanying rewards, which can jeopardize the long-term goals and sustainable orientation of the company.

The time after the attempt can be considered as the beginning of regulation in the field of remuneration. i. Dot-com balloon in the USA. The bankruptcy of some of the major technology giants occurred in the early 21st century, and the main reason was the high indebtedness of these companies, which borrowed at a price below market. The bursting of the bubble led to the write-off of more than 50% of these loans, and the public began to rightly wonder why such an unfolding took place. Cases such as WorldCom (also Enron, Parmalat,…) came to the fore, in which the CEO borrowed money from the company he ran for stock trading.

To prevent the economy from collapsing and restoring confidence in the market, the US Congress passed the Sarbenes-Oakley Act[12] in 2002, which, along with the unification of financial reporting standards, introduced the obligation to adopt corporate governance codes and limit the remuneration of corporate governance bodies. The ratio between the average salaries of employees and members of management bodies has fallen sharply. The new law prohibited companies from taking out loans to finance or credited members of boards of directors and administrations. There is also the possibility of so-called reimbursement, which means that the company can claim back the paid reward to a member of the management body if it proves that the results were different from expectations, or if there has been misleading investors (Tomić et al., 2018). The law, which stopped the uncontrolled growth of earnings, did not only affect American companies, it applied to all companies listed on the American stock exchange, which also covered many companies from the EU.

The test of the effectiveness of the legislation took place in 2008, after the »real estate bubble burst«, which also led to a large reduction in the average remuneration of administrations, which had previously started to rise dramatically again. The answer was again stricter legislation. In 2010, the Dodd-Frank Act was thus enacted, prescribing t. i. say on pay (talk on pay) principle. This allows the company's shareholders to organize and vote at any time on the adequacy of the company's remuneration. Such regulations in the United States also gave rise to EU directives dealing with shareholders' rights and the remuneration of management and supervisory bodies in companies (supra in more detail).

3.1 Remunaration policy under the slovenian companies act (ZGD-1K)

SRD II has re-regulated issues related to the remuneration of management and supervisory bodies, while also upgrading the solutions in the above-mentioned recommendations of the European

[12] An Act to protect investors by improving the accuracy and reliability of corporate disclosures made pursuant to the securities laws, and for other purposes. Public Law 107–204–JULY 30, 2002.

Commission. The essential novelty was regulated in Articles 9a and 9b, which introduce two acts, i.e. the directors ,remuneration policy and the shareholders' right to vote on remuneration policy and the remuneration report and the information to be provided and the right to vote in this regard.

In view of the above, we can conclude that the current regulation in ZGD-1 was compared to e.g. German or Austrian regulations more in line with or closer to the solutions of the SRD II (because Slovenia has enacted some solutions from the recommendations of the European Commission from 2010 and 2011, while Germany and Austria have not legally regulated and changed this) (Bratina, U., 2020).

With the amendment to ZGD-1K, the area of remuneration of members of management and supervisory bodies has been fully harmonized with the SRD II (Articles 9a and 9b), using the appropriate possibilities provided by the Directive in this regard. Nomotechnically, this was done by amending Article 270 of ZGD-1 regarding the remuneration of members of the Management Board, Article 284 regarding payment to members of the Supervisory Board and by amending Article 294 regarding discharge. For implementation, the (most important) new articles have been added, namely Article 294.a (remuneration policy) and Article 294.b (remuneration report), which define all components of the remuneration policy on the one hand and the remuneration report on the other. According to the amendment, public listed companies are obliged to adopt a policy of remuneration of members of management and supervisory bodies at least every four years, which is voted on by shareholders at the general meeting of the company.

The new Article 294.a implemented the provision of Article 9a of the SRD II - on the right to vote on remuneration policy. The essence of the regulation is that public joint stock companies must form a remuneration policy for all members of management and supervisory bodies as well as executive directors who do not otherwise have the status of management under Article 10 of ZGD-1, in accordance with the SRD II however, they are among the directors. So far, ZGD-1 has allowed joint stock companies to determine the remuneration policy, but it has not commanded this. According to the SRD II however, public limited companies have an obligation to formulate a remuneration policy. For non-public joint stock companies (as well as for other capital companies), the policy in question remained the subject of an autonomous decision of the company's bodies.

The new legislation, in accordance with the option provided by the SRD II, defines the consultative nature of the General Meeting`s vote on the remuneration policy. As in Germany, the question arises in our literature as to whether such a transfer of remuneration powers and the conditions of employment of managers to shareholders does not interfere excessively with the role of the supervisory body and thus reduces the effectiveness of management supervision (Kocbek, 2019). In principle, the cogent regulation with ZGD-1 could pose a problem in placing it among the competencies of individual bodies in the company, but the legislator, using the words »Company … formulate …« And »… in the vote to the General Meeting for approval, gave a clear message«, that the proposer and initiator of such a remuneration policy may also be left to any other body, leaving the further implementation to an autonomous regulation (more precisely infra).

Determining the remuneration policy after the company's general meeting has not been a very common business practice so far. Under the new regulation, however, it is important that in the event of a general meeting rejecting the remuneration policy, only the temporary remuneration regime in accordance with the proposed policy applies (coherently), with an amended remuneration policy to be submitted immediately at the next general meeting (third paragraph 9.a Article of the SRD II). The provision of Article 294.a of ZGD-1 does not in any way interfere with other provisions of the law that determine the competencies of individual bodies and other material issues, including regarding remuneration (eg the provision of Article 284 of ZGD-1, which prohibits the participation of members of the Supervisory Board at a profit).

In addition, it is stipulated that a company whose securities are traded on a regulated market shall submit its remuneration policy to the vote at each significant change, and in any case at least every four years.

The new regulation also abandoned the definition of the principles of remuneration policy, as well as what it should be, leaving it to companies that will formulate policy on the basis of guidelines that already appear as drafts of an autonomous legal source (Guidelines on the standardized presentation of remuneration). report under Directive 2007/36/EC, as amended by Directive (EU)

2017/828 as regards the encouragement of long-term shareholder engagement[13]). The legislator only stipulated that the remuneration policy should show in a clear and understandable way in relation to individual components of remuneration e.g. the contribution of remuneration to the promotion of business strategy, long-term development and sustainability of the company. The content of the remuneration policy is specified and the necessary components are listed and their description required for an adequate remuneration policy (eg all fixed and variable remuneration components) (including all allowances and other benefits in any form) and their relative share in the remuneration; all financial and non-financial benchmarks (where applicable as regards social responsibility) for the allocation of variable remuneration components, including an explanation of how these criteria contribute to the promotion of business strategy, long-term development and sustainability of the company and presentation of methods used to determine eligibility; deferral of payment and determination of the conditions that can be met for the company to claim a variable remuneration, in the case of payment of remuneration in the form of shares: periods of allotment, conditions for holding shares after acquisition (if any) and an explanation business strategy, long-term development and sustainability of society; an explanation of how the remuneration and employment conditions of the employees were taken into account in determining the remuneration policy, including an explanation of which group of employees was involved; presentation of the process of determining and implementing and reviewing remuneration policy, including measures to prevent or manage conflicts of interest; in the event of a change in the remuneration policy, an explanation of any significant changes and a review of the extent to which shareholders' votes and opinions regarding the remuneration policy and the remuneration report have been taken into account, etc.).

An important message of the third paragraph of Article 294a of the ZGD-1 is that the voting on the remuneration policy at the General Meeting of Shareholders is of a consultative nature, even though the proposal originally provided for a binding resolution. (Kocbek, M. 2021, p. 1081) A similar technique can be found

13 Available at: https://ec.europa.eu/info/sites/default/files/rrg_draft_21012019.pdf.

in German law[14] (par. 120a dAktG). This is extremely important especially for the company's supervisory board, which with such a solution has retained the powers (including responsibility) for determining remuneration and formulating remuneration policy, and the general meeting somehow »forms« (grants) a non-binding opinion on the prepared remuneration policy. In this way, the concept of different interests of bodies in a joint stock company and delimitation of interests in the company and the company was fully realized[15] (Kocbek, 2021: 1082).

If the General Meeting of Shareholders does not approve the proposed remuneration policy, the company shall submit the amended policy to the vote at the next General Meeting of Shareholders. However, the company may determine the remuneration of the members of the management and supervisory bodies and the executive directors only in accordance with the remuneration policy, which was submitted to the vote for approval at the general meeting. This norm coherently resolves cases where the remuneration policy has not been approved, and at the same time obliges the proposer (supervisory board) to submit an amended and adjusted act of remuneration policy to the next general meeting, without explicitly mentioning what changes should be made. following the German model, in principle, changes are not even necessary if the supervisory board has sufficient arguments for such action) that these can be kept to a minimum (Kocbek, 2021: 1082).

Thus, at the general meeting of the company, the remuneration policy can only be approved or rejected, and a simple majority in concluding the represented share capital is sufficient for such a decision, as it is a normal resolution. Of course, in accordance with ZGD-1, it is necessary to place the decision on the remuneration policy on the agenda of the General Meeting and submit an appropriate resolution proposal, which can be immanently formed only by the Supervisory Board or the Board of Directors. permissible.

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14 Germany and Austria, for example, regulate share law in separate laws - each in its own Share Act (Aktiengesetz, 'dAktG' and 'aAktG'). Both laws regulate only a joint stock company, not other companies.

15 German law expressly provides that the resolution of the general meeting in question does not create any legal consequences and obligations (first paragraph of paragraph 120a d of the AktG) and cannot be challenged. In relation to the Supervisory Board, the Supervisory Board has no legal remedy against the non-approval of the decision on remuneration policy.

Thus, the General Meeting cannot change the proposed remuneration policy and a similar solution was taken as in the case of the adopted annual report and its discussion at the General Meeting. Therefore, the resolutions of the General Meeting that would change the submitted remuneration policy would be null and void, nor would the resolutions that would partially change or approve the remuneration policy be valid, as it is considered as a whole for all members of management and supervisory bodies and executive directors. cannot be shared. Therefore, it can be concluded that the systemic Article 294.a of ZGD-1 (despite the fact that it appears under the section of the law: Powers of the General Meeting) does not interfere in any way with the distribution of powers of bodies in a joint stock company and does not change the concept of ZGD-1 and coherence arrangements in a two-tier management system, thus leaving the autonomy of formulating and determining policy to the supervisory board, which in fact also performs the personnel function in the appointment of management.

Additionally, in 294. a Article ZGD-1 stipulates that a company may temporarily withdraw from the remuneration policy in exceptional circumstances, which cover only cases where this is necessary for the realization of the long-term interests and sustainability of the company as a whole or for securing its assets, if the policy contains procedural conditions. under which a derogation may be applied and provisions on which policy elements may be derogated from. As a sign of a public event, the fifth paragraph of Article 294.a of ZGD-1 stipulates that after voting on the remuneration policy at the General Meeting, it is immediately published on the company's website, together with the date and results of voting, where it must remain free and publicly available for at least as long as it is used, and for at least ten years (ZGD-1K, 2021).

3.2 Remuneration policy report

An important part of the SRD II is communication and improving the relationship with the company's shareholders. Communication can take place on an ongoing basis, but most often companies use it through an annual report, which is presented at the general meeting. For companies with a very compact ownership structure, the annual report is a mere formality and is often intended more for the external public than for shareholders, as shareholders mostly already have their representatives on supervisory boards. For companies with dispersed ownership, the annual report is an important bridge for maintaining relationships and informing shareholders about the company's operations, vision and strategic decisions (Kocbek et al., 2018).

ZGD-1K regulated the scope of the remuneration report for companies whose securities are traded on the regulated market, which must prepare a clear and comprehensible remuneration report, which contains a comprehensive overview of remuneration, including all benefits in any form provided by the company provided or owed to an individual member of the management and supervisory body and to the executive director in the last financial year, in accordance with the remuneration policy.

The preparation of the remuneration report is the responsibility of the members of the management and supervisory bodies and the executive directors, and the remuneration report itself must be reviewed by the auditor, who prepares the report attached to the remuneration report. The report on remuneration is submitted to the General Meeting in the same way as the annual report. The General Meeting has the right to hold a consultative vote on the remuneration report for the last financial year (same rules as for the remuneration policy - supra in more detail). The company must immediately publish the report on remuneration after the vote at the general meeting on the company's website, where it must remain free and publicly available for at least ten years. Ten years after the company's publication in the remuneration report, they no longer provide public access to the personal data of members of management and supervisory bodies and executive directors.

In addition to the personal names of individual members of the management and supervisory body and the executive directors, the remuneration report itself must contain the following information, if any (Bratina, U., 2020):

– total remuneration granted or paid, broken down by component, relative share of fixed and variable remuneration, an explanation of how total remuneration is in line with the adopted remuneration policy and also how it contributes to the company's long-term performance, and information on how performance criteria have been applied;

- the annual change in remuneration, the performance of the company and the average remuneration of full-time employees of the company for that period, for at least the last five financial years, presented together in a way that allows comparison;
- all receipts from any company in the same group;
- the number of shares and stock options provided and the main conditions for exercising the rights, including the exercise price and date and any changes to these conditions;
- whether and how the possibility of reimbursement of variable remuneration has been used;
- any derogations from the procedure for implementing the remuneration policy, and in particular derogations due to exceptional circumstances, including an explanation of those derogations and the definition of the specific elements of the remuneration policy from which they have been waived.

With regard to the remuneration of each individual member of the Management Board (including the Executive Director), the remuneration report must also contain details of financial benefits or benefits or services which:

- they have been approved or provided by a third party to a member of the Management Board in connection with his activity as a member of the Management Board;
- have been approved to a member of the Management Board in the event of early termination of office, including changes agreed in the last financial year;
- were approved to a member of the Management Board in the event of regular termination of office, with the monetary value and the amount spent or reserved by the company in the last financial year, including changes agreed in the last financial year;
- were granted in this connection to a former member of the Management Board whose term of office was terminated in the last financial year and provided in the last financial year.[16]

16 The fact is that due to the limitations of ZGD-1 (especially Article 284), the data between members of management bodies and executive directors and members of supervisory bodies in Slovenia will be very different in amount, as the law prohibits members of the Supervisory Board from participating in profits.

The remuneration report may not include specific categories of personal data on individual members of management and supervisory bodies and executive directors within the meaning of EU GDPR rules[17] or personal data relating to the family situation of individual members of management and supervisory bodies and executive directors.

3.3 Necessary changes to autonomous sources

Due to the amendments to ZGD-1, which improved the notion of remuneration policy and remuneration report, it will be necessary to introduce (adapt) provisions de lege ferenda into the Code, which will clearly define remuneration policy as follows from Article 294.a, and the remuneration report from 294. b Article of ZGD-1. In addition, the preparation of the policy itself and consequently the reports will have to take into account already established (international) guidelines and recommendations in this area. on this basis. These should take into account the legislative framework and the company's good practice and specifics for policy-making and reporting, so that a document defining the company's commitments regarding the remuneration of management and supervisory bodies and executive directors can be developed. In doing so, the remuneration policy should, for example, be clear and comprehensible, with a detailed description of all components of fixed and variable remuneration with all allowances and benefits. It should include pre-defined criteria for financial and non-financial performance and methods for determining whether these criteria are met. Remuneration policy should therefore define how an individual remuneration contributes to the promotion of the business strategy, long-term development and sustainability of the company. As follows from ZGD-1, such a remuneration policy should be submitted to the Assembly for voting at each significant change, or in any case after the expiration of four (term) years. Consequently, the remuneration

17 Determined by Article 9 of Regulation (EU) 2016/679 of the European Parliament and of the Council of 27 April 2016 on the protection of individuals with regard to the processing of personal data and on the free movement of such data and repealing Directive 95/46/EC (OJ 2016 L 119 of 4 May 2016, p.1).

report should be a document containing a comprehensive overview of the remuneration of management and supervisory bodies and executive directors, including any benefits in any form granted or owed to individual directors in the last financial year, including new employees and former directors, all in accordance with the company's remuneration policy. The preparation of the remuneration report will be the responsibility of the members of the management and supervisory bodies and the executive directors, and will have to be reviewed by the auditor and a report on the review will be attached to the remuneration report.

Thus, due to the legal change, it will be necessary to revise and supplement the provisions of the Corporate Governance Policy Framework with a separate chapter Remuneration Policy (in the Code), which will have to clearly define and highlight the corporate phrase that the company's Supervisory Board formulates remuneration policy. legislation and recommendations of good practice in this field and put it to the vote of the Assembly for approval, the Assembly resolution being of a consultative nature only. Based on the wording of Article 294.a of ZGD-1, it will be necessary to regulate all important legal postulates, namely that if the general meeting does not approve the proposed remuneration policy, the company must submit the amended remuneration policy to the next general meeting. In the meantime, the company can only pay out receipts that have been submitted for voting to the general meeting, regardless of whether they have also been accepted. Remuneration policy will have to establish a clear separation between management and supervisory bodies and must be adapted to the situation in the company and the market, so as to promote the company's long-term sustainability and ensure that remuneration is in line with the results achieved and the company's financial situation. Remuneration policies cannot be substantially changed without a presentation and proposal to the general meeting. However, the company is expected to put its remuneration policy to the vote at each significant change, and in any case at least every four years. Allowable changes that are not essential could be e.g. technical changes to the remuneration decision-making process or changes in terminology related to remuneration policy, etc. The company could temporarily and exceptionally deviate from the remuneration policy under certain legal conditions, and must immediately publish on its website the remuneration policy, the result of the General Meeting's vote and the report on remuneration in the last financial year. The remuneration policy and the remuneration report should be free of charge and publicly available for at least as long as they apply, ie. at least ten years.

In addition to the amendments to the Code, it will be necessary to prepare additional autonomous rules - guidelines for the preparation of a report on remuneration policy on the model of foreign practices. In fact, based on Article 9.b of the SRD II, the task of the European Commission is to prepare guidelines for the preparation of the remuneration report of members of management and supervisory bodies and executive directors, which will certainly be the basis and framework for and later implementation in Slovenia as well. The purpose of the guidelines is to provide balanced and flexible guidelines for reporting individual director remuneration in order to enable not only shareholders but also potential investors and stakeholders to assess the remuneration of directors, the extent to which these remuneration is related to the company's performance and thus how the company implements the remuneration policy in practice. The guidelines are intended to take full account of the interests of shareholders, potential investors, other stakeholders and different companies, but are not aimed at a »one-size-fits-all« approach.

Thus, in addition to legal and amendments to the Code, it will be necessary to prepare some novelties in Slovenian corporate practice, such as guidelines based on legal articles and draft non-binding European guidelines modeled on the Finnish Code, which is the only foreign code to include this content. Thus, it contains a series of tables that will be needed for the standardization of remuneration reporting under Article 294.b of ZGD-1. The approach to formulating guidelines is likely to be similar to the current practice in corporate governance, so that they will be prepared for public limited companies, with the reference that they are also applicable to other joint stock companies, or other capital companies, if they decide to use them with defined by society (soft law hierarchy). The guidelines are likely to provide, based on existing models, the legal basis for their applicability, the remuneration policy process itself (from the competences of the authorities, through the content (detailed description) of the policy, the remuneration policy decision-making process and the final publication process), the adoption and publication of a report following the remuneration policy.

In parallel with the recommendations and guidelines of the drafters and trustees of the Slovenian Code for Public Limited Companies, the Slovenian State Holding (SSH) will probably provide its recommendations and guidelines in this area, which will most likely present more binding recommendations for remuneration policy. Although he will have to follow Article 294.a of ZGD-1, he will probably be more detailed about his expectations for what policies he will vote in general meetings in accordance with his code, which is binding on companies with majority state ownership.

4. Conclusions

Data on disclosures of remuneration of management and supervisory boards have been improving in Slovenia since the amendment to the nominal and structural disclosure of remuneration in ZGD-1C in 2009. Despite the recommendations of the Code, none of the Slovenian companies disclosed the remuneration policy, which would explain the performance criteria, set goals and their weights for calculating the variable part, thus enabling shareholders to understand how the company's results are related to the remuneration of board members. supervision). In Slovenia, the largest change in the field of managers ‚salaries was also noticeable in the abandonment of managers' payments from profits (for tax reasons and poorer business results), but there are still no long-term incentives in the structure of management remuneration to encourage long-term sustainable business success. The acceptability of payments with ownership shares or rights to them is declining due to the current economic circumstances. Due to current and past non-disclosures (or limited disclosures), we also do not know whether newer reward mechanisms are in place, such as deferred bonuses, maluses and »clawback clauses«. These stem from regulatory requirements in the banking and financial sectors, but have also been applied in other industries in companies and ensure that bonus payments are carried over to periods when decision results are shown: for loss-making decisions, bonuses are does not pay out, and in cases where there are changes in accounting methods and policies or errors, bonuses are claimed back (Kravanja Novak et al., 2013).

Despite the actual and useful value of the introduced corporate tools for improving corporate governance and appropriate placement in the existing legal framework and competencies of individual bodies, some ambiguities should not be overlooked, which could have negative applications, especially on Slovenian soil. First of all, we would point out the non-regulation or non-classification of procurators in the concept of remuneration of procurators in public joint stock companies. If we highlight their current role and importance and some inappropriate corporate practices, of course their non-inclusion in the remuneration policy can become a problem, as following the current practice, where persons who either did not meet the conditions for appointment to the position of procurators (proxies) corporate function of management, either they did not want corporate responsibility (purely obligatory, which is milder) because their remuneration policy will be able to deviate from the adopted policy at the general meeting. Given the fact of an inconsistent understanding of the position of procurator as a proxy and by attributing managerial powers to this corporate article, there is a great fear of circumventing the rules. Therefore, we believe that it will be necessary to place procurators autonomously within the company's rules, both in terms of remuneration policy and in terms of its reporting.

In general, we can conclude that Slovenian corporate legislation has exemplary (following the example of comparable corporate systems) implemented the SRD II into its national legal order and thus satisfy all the various doctrinal interests and the division of competences of the bodies in society. In addition, such a tool of remuneration policy and its reporting will need to be consistently transposed and included in the Code and the preparation of guidelines, samples and other recommendations that will give companies (in addition to public limited companies) sufficient basis and potential to develop a set of adequate remuneration policies depending on the promotion of business strategy, long-term development and sustainability of the company. Taking into account additional proposals for the placement of tax-friendly treatment, the remuneration policy can also become a key tool for Slovenian companies to ensure a competitive corporate environment in the EU.

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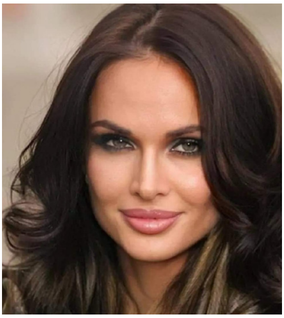

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This monograph is a collection of contemporary critical views on corporate governance in the 21st century in terms of both, social responsibility and sustainable development, as well as efficiency and adaptation to modern business flows. A series of anachronisms is identified, which has emerged due to clinging on to classical property rights approaches and neglecting civilizational challenges, whose shared feature is that the value relations between the increasingly dominating highly intellectual work and capital in modern society are changing rapidly.

Researchers, practitioners and the general public will find the monograph to be an interesting read, especially those who have followed corporate governance developments in recent decades and are looking for development solutions better suited to the rapidly changing business approaches enabled by the digitisation of business life and required in the green transition. We hope the innovative suggestions made in the monograph encourage policymakers to introduce measures to overcome the shortcomings and controversies in corporate governance.

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