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LIABILITY FOR ESG REPORTING OBLIGATIONS IN THE EUROPEAN UNION: POSSIBILITY OF AN INSURANCE COVERAGE

Dissertation to obtain a Master's Degree in Law, in the specialty of Law and Financial Markets.

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ANTI-PLAGIARISM STATEMENT

I hereby declare that the work I present is my own work and that all my citations are correctly acknowledged. I am aware that the use of unacknowledged extraneous materials and sources constitutes a serious ethical and disciplinary offence.

RODRIGO ACILIO BREDA FERREIRA DOS REIS

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QUOTING AND OTHER CONVENTIONS

This Dissertation complies with norm NP 405 of the *Instituto Português de Qualidade* for citations and bibliography. The adopted in-text citation style is that of (AUTHOR, year of publication, page), and direct quotes are written in italic between quotation marks. The complete reference for each source is in the Bibliography section of the Dissertation.

DECLARATION OF CHARACTERS

I hereby declare that the body of this Dissertation has a total of 91.047 characters, including spaces and notes.

RESUMO

Esta Dissertação de Mestrado propõe uma análise da legislação da União Europeia a respeito de temas ESG – *Environmental, Social and Governance* – especialmente no tocante a obrigatoriedade de se incluir nas demonstrações financeiras e no relatório de gestão informações a respeito do impacto que as atividades de determinada empresa têm em questões de sustentabilidade, bem como a influência que questões de sustentabilidade exercem no desenvolvimento das atividades da empresa. Com isso, é possível identificar os agentes responsáveis pelo cumprimento das obrigações impostas pela legislação Europeia e os riscos envolvidos em caso de não cumprimento. Por fim, é discutida a possibilidade de se adquirir um produto de seguro a fim de se proteger contra eventuais impactos financeiros que uma situação de não cumprimento com tais obrigações acarretaria aos responsáveis identificados anteriormente.

Palavras-chave: União Europeia. ESG. Sustentabilidade. Demonstrações Financeiras. Relatório de Gestão. Responsabilidade. Seguro.

ABSTRACT

This Master's Dissertation proposes an analysis of the European Union legislation on ESG – Environmental, Social and Governance – topics, especially with respect to the obligation to include in the financial statements and management report information regarding the impact that the activities of a given undertaking have on sustainability issues, as well as the influence that sustainability issues exert on the development of the undertaking's activities. It will be then possible to identify the persons responsible for complying with the obligations imposed by European legislation, as well as the risks involved in case of non-compliance, followed by a discussion regarding the possibility for the persons identified above to purchase an insurance product to protect themselves against financial impacts that a situation of non-compliance with the legislation would entail.

Keywords: European Union. ESG. Sustainability. Financial Statements. Management Report. Responsibility. Liability. Insurance.

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1. INTRODUCTION

When one considers undertakings operating in the European Union and their obligations when it comes to information they must provide to their stakeholders – especially their own shareholders, the State and the public in general – it is possible to find that their financial statements and its accompanying report, namely, the management report, are at the very centre of all the relevant documents they must prepare and publish to fulfil their information obligation.

This obligation derives from two main pieces of legislation currently in force in the European Union: Directive 2004/109/EC of the European Parliament and of the Council of 15 December 2004, on the harmonisation of transparency requirements in relation to information about issuers whose securities are admitted to trading on a regulated market, published in the Official Journal of the European Union on December 31, 2004 (the "Transparency Directive"), and the Directive 2013/34/EU of the European Parliament and of the Council of 26 June 2013 on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings, published in the Official Journal of the European Union on June 29, 2013 (the "Accounting Directive").

Both the Transparency Directive and the Accounting Directive have gone through changes along the years to accommodate social and political developments regarding new requirements and expectations from parties interested in an undertaking's financial information. One of the most recent and relevant developments in this sense is the increased preoccupation with corporate responsibility and sustainability issues.

This does not come in an isolated context. These preoccupations are directly linked to the rise in Environmental, Social and Governance ("ESG") awareness among institutions, politicians and the civil society in general, which have become increasingly interested in how companies and undertakings across all sectors of the economy not only impact the environment and the societies they operate in, but also how environmental and societal concerns impact their own activities.

As noted by the literature, investors might also consider ESG factors and sustainability reporting as indicators of good governance, since they enhance the public perception of how a certain undertaking performs in sustainability matters, strengthening its reputation and financial performance (DIAS, 2022, p. 223).

In order to address these concerns, the European Union has enacted in recent years various pieces of legislation amending or complementing said Directives to include provisions regarding how ESG information shall be disclosed by undertakings in the context of their financial statements and management report. It is argued in the literature that the intention of the European Union was, essentially, to increment the demand for sustainability-related information among not only institutional investors, but also among the public, through implementing mandatory disclosure rules regarding this information, while indirectly creating an incentive for companies to "behave": "*who wants to announce far and wide their doubtful behaviours on environmental or social issues?*" (ROLO, 2022, p. 207).

Four pieces of legislation in particular stand out as the main acts issued by the European Union to address disclosure obligations of undertakings operating in a territory of a Member State, which are the commonly cited pieces of legislation in the available literature (ROLO, 2022, p. 193; FRADE and FROMOUTH, 2022, p. 238). These are, in chronological order of publication in the Official Journal of the European Union:

1. Directive 2014/95/EU of the European Parliament and of the Council of 22 of October 2014, published in the Official Journal of the European Union on November 15, 2014 (the "Non-Financial Reporting Directive" or "NFRD");
2. Regulation (EU) 2019/2088 of the European Parliament and of the Council of 27 November 2019, published in the Official Journal of the European Union on December 9, 2019 (the "Sustainable Finance Disclosures Regulation" or "SFRD");
3. Regulation (EU) 2020/852 of the European Parliament and of the Council of 18 June 2020, published in the Official

Journal of the European Union on June 22, 2020 (the "Taxonomy Regulation"); and

4. Directive (EU) 2022/2464 of the European Parliament and of the Council of 14 December 2022, published in the Official Journal of the European Union on December 16, 2022 (the "Corporate Sustainability Reporting Directive" or "CSRD").

The only versions of legal texts considered for the purposes of the analysis conducted in this Dissertation are the ones published in the Official Journal of the European Union until May 1, 2024.

The purpose of the present research is to understand how the European Union legislation concerning ESG topics affects undertakings' and/or their administrative, management or supervisory bodies' responsibility and liability for reporting sustainability-related information in their financial statements and management report, and how these undertakings and/or their administrative, management or supervisory bodies could protect themselves against the risk of non-compliance with such responsibilities by means of an insurance coverage.

The main research questions to be answered throughout this Dissertation are the following: (i) What are the risks resulting from the non-compliance of an undertaking or of members of its administrative, management or supervisory bodies, to the new European Union legislation concerning ESG-reporting obligations? (ii) How can these actors protect themselves from these non-compliance risks by means of an insurance coverage? (iii) Is there an existing insurance coverage that could protect them against such risks, or is a completely new, "ESG insurance" coverage needed? (iv) If that is the case, what would be the characteristics of such coverage?

Out of the abovementioned four pieces of legislation, only three, however, have indeed impacted how undertakings in the European Union shall prepare and disclose sustainability-related information in the context of their financial statements and management report, and these are, as further discussed in this Dissertation, the NFRD, the Taxonomy Regulation and the CSRD.

The SFDR will not be analysed in the context of this Dissertation because, as stated in its Recital 10, it deals primarily with certain undertakings' disclosure responsibilities regarding financial products towards end investors that purchase such products, especially disclosures of pre-contractual nature, aiming at facilitating an end investor's understanding of how effectively sustainable a given financial product really is. It does not impact an undertaking's reporting obligations in the preparation and publishing of its financial statements and management report, and, thus, an analysis of this Directive does not contribute to this Dissertation's research purpose.

To achieve the research goal, an analysis of the main changes that the NFRD, the Taxonomy Regulation and the CSRD brought to the Transparency Directive and to the Accounting Directive will be conducted in the Chapter "2. ESG Reporting Legislation in the European Union: an Overview", focusing on reporting obligations concerning the preparation and publishing of financial statements and management reports.

This is necessary to identify what kind of responsibility arises from such obligations and, thus, the risks involved in non-compliance with them. This will be achieved in Chapter "3. Responsibility for ESG Reporting Obligations". From a better understanding of these risks, it will be possible to discuss if undertakings, or members of their administrative, management or supervisory bodies, could protect themselves against these risks by means of purchasing an insurance product.

In Chapter "4. Liability for ESG Reporting Obligations: Possibility of an Insurance Coverage", a general overview of insurance is then presented, thus equipping the analysis with the necessary legal tools to proceed with the discussion regarding the best suited insurance product to insure against the risks associated with non-compliance with the European Union legislation concerning ESG reporting obligations.

Finally, a conclusion for this research is achieved by determining if existing insurance products, and which ones, could work as a risk management and risk mitigation tool regarding ESG reporting in the European Union to be used by the actors subject to these obligations.

The analysis will primarily consider the European Union legislation indicated above (NFRD, Taxonomy Regulation and CSRD), with the support of specialized literature developed about the subjects herein discussed. Subsidiarily, legislation from Portugal may also be analysed, if it contributes to the understanding of a certain topic, as well as the Principles of European Tort Law, prepared by the European Group on Tort Law, and the Principles of European Insurance Contract Law, prepared by the Project Group Restatement of European Insurance Contract Law.

2. ESG REPORTING LEGISLATION IN THE EUROPEAN UNION: AN OVERVIEW

As mentioned in Chapter “1. Introduction” of this Dissertation, the first step of this analysis is an investigation and exposition of legislation enacted by the European Union regarding ESG reporting obligations, that is, the NFDR, the Taxonomy Regulation, and the CSRD. For didactic purposes, the analysis will follow the chronological order of publication of these pieces of legislation in the Official Journal of the European Union.

As further explored below, when the NFRD was enacted, the article of the Accounting Directive relevant for stablishing the responsibility regime for reporting obligations had a different wording than the version of the text effective in May 1, 2024. This is because the CSRD, when it was enacted, changed the wording of this article. The differences in the text are very relevant for the analysis to be conducted in this Dissertation and will be discussed accordingly.

2.1. NFRD

The self-proclaimed aim of the NFRD, declared in its Recitals 1 and 3, was to increase “*transparency of social and environmental information provided by undertakings*” in the European Union in order to “*identify sustainability risks and increase investor and consumer trust*”.

The main change implemented by NFRD, as per its Recital 6, was making it mandatory for some large undertakings to include a non-financial statement in their management report, or to prepare a separate non-financial report, containing information related to environmental, social, labour, human rights, anti-corruption and anti-bribery matters, in which these undertakings should describe the policies adopted by them, including due diligence processes, to properly manage (identify, prevent and mitigate) sustainability risks associated with those matters.

The most important modifications the NFRD brought to the Accounting Directive were: (1) the addition to the Accounting Directive of two new articles concerning the drafting and publication of non-financial information, Articles 19a and

29a, and (2) the inclusion of information concerning diversity to be provided in the corporate governance statement already foreseen in Article 20 of the Accounting Directive.

Article 19a explicitly stipulates that the entities that became obliged to include a non-financial statement regarding sustainability matters in their management report were only large undertaking which are public interest entities – defined in Article 2(1) of the Accounting Directive as undertakings whose transferable securities are admitted to trading on a regulated market, credit institutions, insurance companies, and other undertakings classified as such by Member States of the European Union – and which had an average number of more than 500 employees during the financial year. The justification provided in Recital 13 of the NFDR for the adoption of these new rules only to large undertakings was the "*think small first*" principle, which claims that small and medium-sized enterprises could suffer in productivity terms from this increased regulatory burden and should instead benefit first from measures to improve their business environment and internationalisation to promote their growth.

Article 29a, on its turn, set the rules applicable to non-financial information to be provided by a public-interest parent undertaking of a large group that fulfils, on a consolidated basis, the criteria of more than 500 employees during the financial year.

When it comes to diversity, item (g) was added to paragraph 1 of Article 20 of the Accounting Directive to mandate the disclosure, in the corporate governance statement, of policies adopted by undertakings in the composition of their administrative, management and supervisory bodies in aspects such as age, gender, and educational and professional backgrounds. By means of the newly added paragraph 5 to the same Article, this new obligation was also not to be applied to small and medium-sized enterprises, thus limiting its application only to large undertakings as well.

It is noted in the literature how the NFDR was built around the "*comply or explain"* principle (ROLO, 2022, p. 198), in which undertakings that do not adopt policies in relation to sustainability and/or diversity matters, or that wish to omit some information from their non-financial statement or report under some exceptional

cases, were also mandated to provide a clear and reasoned explanation for their decisions. Undertakings are only exempted from drafting a non-financial statement or report if they are a subsidiary and their non-financial information in disclosed by another undertaking which is a member of the economic group.

Undertakings should also specify which framework they would use to disclose their non-financial information, be it a national, Union-based or international framework. Some frameworks mentioned in Recital 9 of the NFRD are: the Eco-Management and Audit Scheme (EMAS); the United Nations (UN) Global Compact; the Guiding Principles on Business and Human Rights implementing the UN 'Protect, Respect and Remedy' Framework; the Organisation for Economic Co-operation and Development (OECD) Guidelines for Multinational Enterprises; the International Organisation for Standardisation's ISO 26000; the International Labour Organisation's Tripartite Declaration of principles concerning multinational enterprises and social policy; the Global Reporting Initiative, among others recognized frameworks.

This demonstrates a non-exhaustive and illustrative approach to recommended frameworks, in contrast to a mandatory list of Union-approved frameworks. NFDR also stipulated in its Article 2 that the Commission should prepare non-binding guidelines on methodology for reporting non-financial information, in addition to the abovementioned frameworks, which was accomplished by means of the publication of Communication from the Commission 2017/C 215/01, on July 5, 2017, subsequently supplemented by Communication from the Commission 2019/C 209/01, that specified some climate-related disclosures in the guidelines.

The text of both Communications stress that their aim is to provide for non-binding guidelines and that they do not create new legal obligations. Both also reinforce that they do not constitute a technical standard of any sort, to the point they alert preparers of non-financial statements and any other party that they should not claim that non-financial statements were in conformity with the guidelines. Throughout these documents, the Commission merely proposes examples and recommendations as to how undertakings could report non-financial information.

These new disclosure obligations became subject to the already existing Article 33 of the Accounting Directive, which, according to its text in effect on the date of publication of NFRD in the Official Journal of the European Union, stipulated that:

> "(…) *the members of the administrative, management and supervisory bodies of an undertaking (…) have collective responsibility for ensuring that*
>
> *(a) the annual financial statements, the management report and, when provided separately, the corporate governance statement; and*
> *(b) the consolidated financial statements, consolidated management reports and, when provided separately, the consolidated corporate governance statement,*
>
> *are drawn up and published in accordance with the requirements of this Directive (…)*"

In this sense, it is possible to affirm that the scope of responsibility of members of the administrative, management and supervisory bodies of undertakings subject to the already existing Article 33 of the Accounting Directive was enlarged to include, for the first time, the reporting obligations introduced by the NFRD. The nature of this responsibility, as well as an analysis of the wording adopted by the regulator in the legal text, is at the very centre of the analysis of this Dissertation and will be discussed in detail in Chapter "3. Responsibility for ESG Reporting Obligations" below.

2.2. TAXONOMY REGULATION

The next major development in ESG reporting in the European Union came with the Taxonomy Regulation, which stipulated in its Recital 5 that it was developed to create "*a technically robust classification system at Union level to establish clarity on which activities qualify as 'green' or 'sustainable', starting with climate change mitigation*", with a clear intent of combating a phenomenon that has come to be

called “*greenwashing*”, that is defined in its Recital 11 as “*the practice of gaining an unfair competitive advantage by marketing a financial product as environmentally friendly, when in fact basic environmental standards have not been met*.”

As stated above, the Taxonomy Regulation was a first attempt at stablishing a framework to enable the identification of activities that could be considered as environmentally sustainable. Social or Governance aspects were not addressed, because, as per cited in its Recital 6, “*Further guidance on activities that contribute to other sustainability objectives, including social objectives, might be developed at a later stage*”.

Reminiscing SFDR, the Taxonomy Regulation deals mainly with financial product and end investor preoccupations, as illustrated in its Recital 18. The analysis of this regulation will, therefore, focus on the changes the Taxonomy Regulation brought to reporting obligations, complementing the previous NFRD and the Accounting Directive.

Article 8 of the Taxonomy Regulation set forth the obligation for undertakings subject to the reporting rules of Articles 19a or 29a of the Accounting Directive, implemented by means of the NFRD, to also include in their non-financial statement or report information on how and to what extent their activities qualify as environmentally sustainable under the terms of the Taxonomy Regulation.

As per Articles 3 and 9 of the Taxonomy Regulation, to qualify as environmentally sustainable, a given activity must either contribute substantially or do not significantly harm the following environmental objectives: climate change mitigation; climate change adaptation; the sustainable use and protection of water and marine resources; the transition to a circular economy; pollution prevention and control; and the protection and restoration of biodiversity and ecosystems.

Non-financial undertakings in particular are subject to a specific set of rules which mandates the inclusion, in their non-financial statement or report, of information concerning the proportion of their turnover, the proportion of their capital expenditure and the proportion of their operating expenditure related to assets or processes derived from environmentally sustainable activities, as per Article 8(2) of the Taxonomy Regulation.

The Commission Delegated Regulation (EU) 2021/2178 of 6 July 2021, published on the Official Journal of the European Union on December 10, 2021, specified the methodology applicable to such reporting obligation. Contrary to the previous approach used by the Commission as to how the information contained in the non-financial statement or report should be conveyed, that is, by recommending a set of frameworks, as well as stablishing its own optional framework that undertakings could adopt by means of Communications 2017/C 215/01 and 2019/C 209/01, this time the Commission made it mandatory for undertakings to adopt the classification criteria related to the environmentally sustainable activities of the Taxonomy Regulation.

It is important to notice that the Taxonomy Regulation did not directly implement any amendment to the text of the Accounting Directive to include the abovementioned reporting obligation set forth in its Article 8 to that Directive. In this sense, one could argue that there could not be established a direct link between the reporting obligation prescribed by the Taxonomy Regulation and the responsibility principle set forth in Article 33 of the Accounting Directive. As discussed below, this was later solved with the CSRD, which implemented the necessary amendments to make this link explicit in the text of the Accounting Directive.

2.3. CSRD

Further developments in sustainability reporting came with the advent of the CSRD, which is the most encompassing sustainability-related reporting regulation approved by the European Union to date, having implemented extensive amendments to a wide range of previous pieces of legislation on the matter.

The self-proclaimed aim of CSRD, enshrined in its Recital 5, is to address a need identified by the European Parliament "*to set up a comprehensive Union framework (…) that contains mandatory Union non-financial reporting standards*". While the previous approach from the EU legislation was to recommend a set of frameworks, the new approach is to make it mandatory for all undertakings to observe a new standard of reporting. This is further reinforced by the mention in Recitals 13 and 37 of a "*clear need for a robust and affordable reporting framework*

that is accompanied by effective auditing practices to ensure the reliability of data and avoid greenwashing and double counting", to the point "*in which sustainability information has a status comparable to that of financial information".*

This comparability of status between financial and non-financial information made the European Commission consider that a change in terminology was necessary: as exposed in Recital 8 of the CSRD, "non-financial information" implicitly means that the information conveyed under such label has no financial relevance, while the opposite had become increasingly true. In this sense, the new terminology adopted is that of "sustainability information". To reflect this change, "sustainability information" will be the terminology used in this Dissertation going forward.

The first major change brought by CSRD is the enlargement of entities that are subject to sustainability reporting obligations. As per the amendments the CSRD implemented to Article 1 of the Accounting Directive, all large undertakings – defined in its Article 3(1), item (c), undertakings which on their balance sheet dates exceed at least two of the three following criteria: (a) balance sheet total: EUR 25 000 000; (b) net turnover: EUR 50 000 000; (c) average number of employees during the financial year: 250 –, and undertakings whose securities are admitted to trading on a regulated market (except if those undertakings are micro undertakings), should be required to report sustainability information.

This was the first time small and medium-sized public interest undertakings, as well as all large undertakings, regardless of whether they are public interest entities or not, became obliged to report sustainability information in their financial statements and management reports.

The information to be reported by small and medium-sized undertakings is the one delineated in the newly introduced paragraph 6 of Article 19a of the Accounting Directive. These undertakings might as well choose not to include sustainability information in their management report, but in this situation, they must justify this option in their management report.

Applicable to all undertakings, CSRD, in its Recital 33, also considered the importance of reporting on forward-looking information, and not only information about past performance. It then introduced a new change in sustainability reporting

obligations to include forward-looking information, both quantitative and qualitative. Paragraph 2 of Article 19a of the Accounting Directive was amended accordingly to reflect such changes, implementing the obligation to report on short-, medium- and long-term scenarios.

The CSRD also made explicit in Recital 29 the adoption of double-materiality perspective in sustainability information reporting, in which undertakings ought to report not only the impact of sustainability matters in their activities, but also the impact their own activities have in sustainability matters. The text of Article 19a(1) of the Accounting Directive was adjusted accordingly.

The CSRD also eliminates the possibility of undertakings to publish their sustainability information in a separate report, as was previously allowed under the terms of the NFRD, because, as explained in its Recital 57, it is understood that the publication of a separate report hinders the findability and reliability of sustainability information.

Some further amendments to the text of the Accounting Directive were the inclusion of new Articles 29b and 29d, that granted powers to the Commission to adopt the necessary measures to define and set the sustainability reporting standards. These standards ought to include, for the first time, a series of factors regarding social, human rights and governance issues. Previously, as per exposed in Chapter “2.2.Taxonomy Regulation”, detailed disclosure standards were only defined for environmental factors, while social and governance factors would be regulated afterwards. CSRD filled this gap by foreseeing, in items (b) and (c) of paragraph 2 of Article 29b of the Accounting Directive, that the Commission ought to regulate these other factors as well, which was done by means of Commission Delegated Regulation (EU) 2023/2772 of 31 July 2023, published in the Official Journal of the European Union on December 22, 2023 (the “European Sustainability Reporting Standards” or the “ESRS”).

For small and medium-sized undertakings, specific standards ought to be adopted by the Commission taking into consideration the scale and complexity of their activities, as per Article 29c. These standards had not yet been published in the Official Journal of the European Union by May 1, 2024.

With the introduction of Article 29d to the Accounting Directive, as well as the implementation of an amendment to the text of Article 33 of the same Directive, the problem cited in Chapter “2.2. Taxonomy Regulation” about the uncertainty of the responsibility for the reporting obligation set forth in Article 8 of the Taxonomy Regulation was solved by means of: (1) explicitly including in the paragraphs 1 and 2 of Article 29d of the Accounting Directive that the sustainability report prepared according not only to Article 19a and 29a of the Accounting Directive, but also to Article 8 of the Taxonomy Regulation, shall observe a mandatory format of reporting, that of the single electronic reporting format; and (2) by amending Article 33 of the Accounting Directive to make it explicit that members of the administrative, management and supervisory bodies of undertakings have collective responsibility for ensuring that sustainability reporting is done according to the format required in the new Article 29d of the Accounting Directive, as per the new implemented text below:

> *“(…) members of the administrative, management and supervisory bodies of an undertaking, acting within the competences assigned to them by national law, have collective responsibility for ensuring that the following documents are drawn up and published in accordance with the requirements of this Directive and, where applicable, with the international accounting standards adopted pursuant to Regulation (EC) No 1606/2002, with Delegated Regulation (EU) 2019/815, with the sustainability reporting standards referred to in Article 29b or Article 29c of this Directive, and with the requirements of Article 29d of this Directive:*
>
> *(a) the annual financial statements, the management report and the corporate governance statement when provided separately; and*
> *(b) the consolidated financial statements, the consolidated management reports and the consolidated corporate governance statement when provided separately.”*

As mentioned previously in Chapter “2.1 NFRD” of this Dissertation, the nature of the responsibility assigned by Article 33 of the Accounting Directive, with the new wording implemented by the CSRD, is at the very centre of the analysis of this Dissertation and will be discussed in detail in Chapter “3. Responsibility for ESG Reporting Obligations” below.

A novelty introduced by CSRD is the inclusion of certain third country undertakings among those who are obliged to provide sustainability reporting in the European Union, which, as per Recitals 19 and 20, aims at “*responding to the needs of financial market participants for information from such undertakings*”, but also to ensure that these undertakings “*are accountable for their impacts on people and the environment and that there is a level playing field for companies operating in the internal market.”*

This was regulated by means of the introduction of Article 40a in the Accounting Directive, which stablished that large subsidiary undertakings, and small and medium-sized undertakings (except micro undertakings) which are public interest entities, that have an ultimate parent undertaking governed by the law of a third country, as well as a branch of an undertaking governed by the law of a third country that is either not part of a group or are ultimately held by an undertaking that is formed in accordance with the law of a third country, should also include sustainability information in their reporting at group level, considering that said third-country undertaking generated a net turnover of more than EUR 150 million in the European Union. Specific reporting standards for these types of undertaking are also applicable, as per paragraph 2 of Article 40a and Article 40b of the Accounting Directive. These standards had not yet been published in the Official Journal of the European Union by May 1, 2024.

Specifically for third country undertakings, a new Article 40c was introduced to the Accounting Directive to define the responsibility for their sustainability information reporting, as per the below:

> *“(…) the branches of third-country undertakings are responsible for ensuring, to the best of their knowledge and ability, that their sustainability report is drawn up in accordance*

with Article 40a, and that that report is published and made accessible in accordance with Article 40d.

(…) the members of the administrative, management and supervisory bodies of the subsidiary undertakings referred to in Article 40a have collective responsibility for ensuring, to the best of their knowledge and ability, that their sustainability report is drawn up in accordance with Article 40a, and that that report is published and made accessible in accordance with Article 40d."

Article 40d, however, does not include any mention to Article 8 of the Taxonomy Regulation. This is done in the second subparagraph of Article 48i(1), which explicitly foresees that until January 6, 2030, subsidiary undertakings of a parent undertaking not governed by a law of a Member State may prepare a consolidated sustainability reporting including the disclosures set forth in Article 8 of the Taxonomy Regulation.

The analysis concerning Article 40c is also at the very centre of the analysis of this Dissertation and will be discussed in detail in Chapter "3. Responsibility for ESG Reporting Obligations" below.

Before following the analysis of the changes implemented by CSRD to the Transparency Directive, it is important to define what is understood as "issuer". Under the terms of Article 2(1), item (d), of the Transparency Directive, "issuer" means a *"natural person, or a legal entity governed by private or public law, including a State, whose securities are admitted to trading on a regulated market"*.

Provided this definition, it is possible to identify the amendments implemented to the Transparency Directive by the CSRD, starting with the replacement of the text of item (c) of Article 4(2) to make it explicit that the "*persons responsible within the issuer, whose names and functions shall be clearly indicated*" must make a statement attesting that the management report *"is prepared in accordance with sustainability reporting standards"* pursuant to the rules defined for such in the Accounting Directive.

CSRD also changed the text of Article 4(5) of the Transparency Directive to include the obligation for issuers of securities admitted to trading on a regulated market in the Union to make public an annual financial report in accordance with Articles 19a, 29a and 29d of the Accounting Directive and with Article 8 of the Taxonomy Regulation.

Article 7 of the Transparency Directive, on its turn, stipulated the issuer or its administrative, management or supervisory bodies, or the "persons responsible within the issuers", as responsible for complying with the obligations set forth in Article 4 of such Directive, that is, responsible for preparing and making public its sustainability report according to the Accounting Directive and with Article 8 of the Taxonomy Regulation, as per the below:

> *"(…) responsibility for the information to be drawn up and made public in accordance with Articles 4 (…) lies at least with the issuer or its administrative, management or supervisory bodies and shall ensure that their laws, regulations and administrative provisions on liability apply to the issuers, the bodies referred to in this Article or the persons responsible within the issuers."*

It is important to note a distinction in wording between the Accounting Directive and the Transparency Directive: while the first explicitly refers to the members of administrative, management and supervisory bodies, the latter mentions that the responsibility for complying with sustainability reporting obligations may lie with the bodies themselves, with no reference to "members", while adding two new actors that might also be responsible for complying with sustainability reporting obligations: the issuers themselves or the "persons responsible within the issuers".

The impact of such distinction, as well as the nature of the responsibility arising from Article 7 of the Transparency Directive, will be analysed in the following Chapter of this Dissertation.

3. RESPONSIBILITY FOR ESG REPORTING OBLIGATIONS

As seen in the previous Chapter, the regulation concerning sustainability information reporting in the European Union also defined the persons responsible for complying with such obligation. The purpose of this Chapter of the Dissertation is to understand the nature of this responsibility.

Concerning undertakings obliged to report sustainability information under the terms of Articles 19a and 29a implemented in the Accounting Directive by means of the NFRD, whose text was amended by the CSRD, one can derive from Article 33 of the Accounting Directive, already existent when the NFRD was published in the Official Journal, and then amended by the CSRD, that the persons responsible are the members of the administrative, management and supervisory bodies of the undertaking. Also of importance is the use of the term *"collective responsibility",* which, as discussed below, brings some doubts as to how it should be interpreted.

The responsibility defined for undertakings subject to Article 40a of the Accounting Directive, on the other hand, is slightly different, since it depends on whether the third country undertaking operates in the European Union by means of stablishing a branch or a subsidiary. As per the text of Article 40c, for a branch the responsibility falls on the branch itself, while in the case of subsidiary undertakings the text is very similar to the one used for undertakings subject to Articles 19a and 29a, that is, that the persons responsible are members of the administrative, management and supervisory bodies of the subsidiary undertaking. In the latter case, the term used is also that of *"collective responsibility"* among the members of these bodies.

Finally, the responsibility regarding sustainability reporting in the context of the Transparency Directive, from what can be understood from its Article 7, may fall on either the issuer itself; its administrative, management or supervisory bodies; or the "persons responsible within the issuers".

For ease of understanding, the analysis will be divided by type of undertaking concerned: undertakings subject to Articles 19a or 29a of the Accounting Directive; undertakings subject to Article 40a of the Accounting Directive; and undertakings subject to Article 4 of the Transparency Directive. When the conclusions reached for

one of these groups may also be applied to others, this will be duly noted and justified.

3.1. UNDERTAKINGS SUBJECT TO ARTICLES 19A AND 29A OF THE ACCOUNTING DIRECTIVE

With regards to the discussion of the responsibility established in Article 33 of the Accounting Directive for these undertakings, which are, as exposed in the previous Chapter of this Dissertation, the undertakings subject to Article 19a of the Accounting Directive – large undertakings, and small and medium-sized undertakings, except micro undertakings, which are public-interest entities –, and those subject to Article 29a of the Accounting Directive – parent undertakings of a large group –, two main issues must be addressed.

The first is understanding the legal nature of such responsibility and its accompanying liability in case of damage, in the sense of understanding if it is of civil, administrative, or criminal nature; contractual or non-contractual (statutory); and whether it is strict or depending on fault. The second is understanding what "collective responsibility" means when it comes to allocating responsibility among members of the administrative, management and supervisory bodies of the undertaking, since this terminology is not commonly used in legal contexts and might bring doubts as to how it should be interpreted.

With regards to the first issue, one must, then, understand whether the responsibility in question is of civil, administrative, or criminal nature. In this sense, one must consider that any breach of the responsibility for complying with the rules set forth in the Accounting Directive may cause damages to third-parties, which might seek indemnification against wrongdoers for their losses (PAOLINI and NAMBISAN, 2014, p. 11). In this sense, the responsibility set forth in Article 33 of the Accounting Directive may be understood as, primarily, a source civil liability, especially when interpreted as a standalone Article.

This is because errors in financial or sustainability information might give to stakeholders a false image of the undertaking's performance, which might, then affect their decisions about how they interact with such undertaking, as in the case,

for instance, of an investor who chooses to invest in a given undertaking only to find that their financial or sustainability information, upon which they had made their decision to invest in the undertaking, was, ultimately, false or wrong. Seeking indemnification for such damage is a matter of civil nature, under the scope of either contractual or tort law. It is important to notice that this Dissertation will ultimately focus on this sort of responsibility, as further explored in the next Chapter "4. Liability for ESG Reporting Obligations: Possibility of an Insurance Coverage".

However, it is important to consider that this responsibility may also encompass administrative and criminal liability when interpreted in conjunction with Article 51 of the Accounting Directive, which mandates Member States of the European Union to "*provide for penalties applicable to infringements of the national provisions adopted in accordance with this Directive and shall take all the measures necessary to ensure that those penalties are enforced*". It may also undertake administrative or criminal aspects when one considers that the error in financial or sustainability information may be caused by fraudulent, deliberate or wilful misconduct. In such cases, the conduct is considered to be a damage not only to private third-parties, but also to the public interest and public good, thus requiring the State to impose administrative (such as penalties) and/or criminal sanctions.

Continuing on the analysis of the first issue, the nature of the responsibility for publishing financial and sustainability information according to the Accounting Directive is ought to be understood as being extra-contractual, that is, not derived from private autonomy of individuals (from contracts), but from the Law, thus being a statutory duty. This is also the understanding of the literature on the subject, which extensively classify the duty of complying with accounting standards, and publishing financial statements and their accompanying management report, as a statutory duty (ABREU, 2013, p. 780, 786, 907, 908; PAOLINI and NAMBISAN, 2014, p. 121, 140; RAMOS, 2010, p. 143).

Finally, there is a diversion in the literature with regards to this responsibility being understood as depending on fault or not (in the latter case, a strict responsibility). The position of understanding this responsibility as strict, that is, irrespective of fault, considers that a breach of a mandatory rule, or a statutory duty, imposed by Law, makes fault irrelevant in determining responsibility (PAOLINI and

NAMBISAN, 2014, p. 140, 142). This is also illustrated by the literature in the case of Italy, for instance, in which dispositions of that country's Civil Code prior to 2003 allowed for an interpretation that would consider all co-administrators of a given undertaking responsible, regardless of each one's effective contribution (fault) to the damage itself, which was later changed by amendments introduced in that Civil Code in 2003 that reformed the responsibility regime of administrators to prevent interpretations of the legal text that allowed strict responsibility of administrators (ABREU, 2013, p. 858, 859; RAMOS, 2010, p. 177).

The majority of the literature, however, understands the responsibility to be depending on fault (ABREU, 2010, p. 7; ABREU, 2013, p. 842, 859, 906, 910; PAOLINI and NAMBISAN, 2014, p. 126; RAMOS, 2010, p. 119, 396). This is because strict responsibility, as understood by the analysed literature, is usually applied only to activities involving some kind of risk to third-parties, even when due care is exercised, or activities which make it impossible to the damaged party to prove the responsibility for the damage (HÖRSTER, 1992, p. 74). Among the activities which have been classified as such are, for instance, blasting, handling of dangerous animals, driving a motor car, commercializing products, or conducting airline transportation (EUROPEAN GROUP ON TORT LAW, 2005, p. 104, 109, 110). Drafting and publishing of financial or sustainability information cannot be considered a risky activity because it has not been explicitly considered as such by the Law, therefore, the general principals of responsibility depending on fault must be applied.

Resolving, thus, the first issue encountered in the interpretation of Article 33 of the Accounting Directive, it is necessary to discuss the meaning of "collective responsibility". As mentioned before, this term is not usually used in legal contexts, which give preference for terms such as "joint" or "several" responsibility when referring to responsibility for one event being attributed to more than one person at the same time. In this respect, the choice for this term demands from those interpreting it an extra effort in understanding what it ought to mean, given its relevance in determining the allocation of responsibility among members of administrative, management and supervisory bodies of undertakings for financial and sustainability information they disclose by means of a financial statement and management report.

As a first step towards better understanding the meaning of this term, it is important to notice that other European Union legislation on financial markets in general do not refer to “members” of administrative, management or supervisory bodies of undertakings, making reference only to these “bodies” themselves.

In order to illustrate the above, three pieces of legislation will be analysed. The first is Directive 2013/36/EU of the European Parliament and of the Council of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions (“Capital Requirements Directive” or “CRD”), which sets forth in its Article 88(1), item (b), that “*the management body must ensure the integrity of the accounting and financial reporting systems, including financial and operational controls and compliance with the law and relevant standards*”.

The second is Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments (“Markets in Financial Instruments Directive” or “MiFID II”) that stipulates in its Article 9(1) that “*competent authorities (…) shall ensure that investment firms and their management bodies comply with Article 88*” of the CRD.

The third piece of legislation to be analysed is Directive 2009/138/EC of the European Parliament and of the Council of 25 November 2009 on the taking-up and pursuit of the business of Insurance and Reinsurance (“Solvency II Directive”), which references, in its Article 40, that “*the administrative, management or supervisory body of the insurance or reinsurance undertaking has the ultimate responsibility for the compliance, by the undertaking concerned, with the laws, regulations and administrative provisions adopted pursuant to*” the Solvency II Directive

In this sense, the reference of “members” of administrative, management and supervisory bodies is exclusive to the Accounting Directive. This seems to be more in accordance with the general understanding that in order for a given person be deemed legally responsible for something, one must assume that this person has legal personality (HÖRSTER, 1992, p. 72-73). Administrative, management and supervisory bodies of an undertaking do not have a separate legal personality than that of the undertaking to which they are part of, making it impossible for such “bodies” to be deemed responsible. Such responsibility must always be understood

as a responsibility for members of such bodies, which have themselves legal personality (be it because they are either legal or natural persons), and, as such, are the only ones capable of being subjects of rights and obligations, and, consequently, of being responsible for their acts and for occasional damages they cause to others (HÖRSTER, 1992, p. 308).

In this regard, “collective responsibility” must necessarily mean that responsibility for financial and sustainability information is shared among individual members of an undertaking’s administrative, management and supervisory bodies (PAOLINI and NAMBISAN, 2014, p. 144). The allocation of each member’s share of responsibility shall be determined by whether responsibility is understood as strict or depending on fault.

This is because, if one understands that responsibility is strict, as pointed by some authors in the literature, each member of the administrative, management and supervisory bodies is equally responsible for the damages caused by their actions, irrespective of each individual member’s fault. If, however, the understanding is that the responsibility depends on fault, each member may only be responsible up to the proportion of their actions with direct relation to the damage. The latter is not only the prevalent opinion in the literature, as explored previously, but is also adopted in the Portuguese Law, by means of Article 73 of its *Código das Sociedades Comerciais*, which assumes members of administrative bodies to be equally responsible for a certain damage, admitting that if they prove otherwise, they must be exempted of responsibility. This assumption is a common feature of civil law jurisdictions (PAOLINI and NAMBISAN, 144).

3.2. UNDERTAKINGS SUBJECT TO ARTICLE 40A OF THE ACCOUNTING DIRECTIVE

Undertakings subject to this Article are large subsidiary undertakings, and small and medium-sized undertakings (except micro undertakings) which are public interest entities, that have an ultimate parent undertaking governed by the law of a third country, as well as a branch of an undertaking governed by the law of a third

country that is either not part of a group or are ultimately held by an undertaking that is formed in accordance with the law of a third country.

The main challenge in discussing responsibility for the preparation and publishing of financial and sustainability information for these entities is that it introduces a new actor that has not been discussed in this Dissertation yet: the branch. This is because the branch is not considered a separate legal entity than its parent undertaking (usually called “head office”), but a “*geographically separate operating unit*” of one parent undertaking (SEGAL, 2022), often consisting of “*smaller divisions of different aspects of the company such as human resources, marketing, and accounting*” (KENTON, 2022), while a subsidiary undertaking is considered a separate legal entity, and, as such, is independently operated from their parent undertaking (KENTON, 2023).

As provided in Article 40c of the Accounting Directive, the rules applicable to branches and to subsidiary undertakings are different: while for subsidiary undertakings the text of the Law makes it explicit that the persons who have “collective responsibility” for drawing up the sustainability report are “*the members of the administrative, management and supervisory bodies of the subsidiary undertaking”,* the responsibility in the case of a branch lies with the branch itself.

In this sense, the conclusions reached in the previous Chapter “3.1. Undertakings Subject to Articles 19a and 29a of the Accounting Directive” are also applicable to subsidiary undertakings of a parent undertaking governed by the law of a third country: that the nature of this responsibility is primarily civil, with the possibility of also assuming administrative or criminal characteristics; that it is extra-contractual, imposing a statutory duty on administrators regarding the preparation of financial and sustainability information; that it is dependent on fault; and that it is shared among administrators found to be at fault, exempting administrators which have not acted on fault.

This is because, having a legal personality of their own, and independent from their parent undertakings, such undertakings must also have administrative, management and supervisory bodies of their own, which will, on their turn, have members which will be responsible from drawing up financial and sustainability information according to the Accounting Directive.

Branches, however, do not have a distinct legal personality than that of their parent undertakings. As also seen in the previous Chapter, “3.1. Undertakings Subject to Articles 19a and 29a of the Accounting Directive”, a fundamental assumption for having legal responsibility is having legal personality. In this sense, branches cannot, themselves, be held responsible for drawing up financial and sustainability information.

It is important to notice that other relevant pieces of legislation enacted by the European Union that regulate the establishment, in a Member State, of a branch belonging to an undertaking with head office in a third country mandate that head offices indicate persons responsible for representing or for managing the branch. That is the case for the CRD, which provides in its Article 47(1a), item (f), that credit institutions must indicate “*key function holders for the activities of the branch*”; for MiFID II, that stipulates in its Article 35(2), item (f), that investment firms must indicate “*the names of those responsible for the management of the branch*”; and for the Solvency II Directive, which mandates that insurance and reinsurance undertakings must indicate a “general representative” for their branches, by means of its Article 162(2), item (d).

Besides these, Directive (EU) 2017/1132 of the European Parliament and of the Council of 14 June 2017 relating to certain aspects of company law (“Company Law Directive”) also sets forth in its Article 37, item (h), that any company governed by the law of a third country must disclose “*the appointment, termination of office and particulars of the persons who are authorised to represent the company in dealings with third parties and in legal proceedings*”.

As discussed above, the Accounting Directive does not mention these individualized persons, be them legal or natural persons, as responsible for publishing financial and sustainability information, instead claiming as responsible the branch itself, which cannot be held responsible because of its lack of legal personality. This may ultimately hinder the ability to effectively hold branches of head offices governed by the Law of third countries accountable in case they fail to disclose sustainability information in their management report according to the Accounting Directive.

In this sense, the text of the Accounting Directive shall be interpreted in conjunction with the terms of the CRD, the MiFID II, the Solvency II Directive, and the Company Law Directive, to necessarily indicate, in a systematic interpretation of the Law (that is, an interpretation that takes into consideration the legal system as a whole, and not individual norms considered in isolation), that these individualized persons indicated to represent or manage the branch of a head office governed by the law of a third country shall be considered the ones responsible for complying with the rules regarding the drawing up of financial and sustainability information.

3.3. UNDERTAKINGS SUBJECT TO ARTICLE 4 OF THE TRANSPARENCY DIRECTIVE

According to Article 1(1) of the Transparency Directive, the undertakings subject to the rules set forth therein are "*issuers whose securities are (…) admitted to trading on a regulated market situated or operating within a Member State*" of the European Union. In this sese, the term "undertaking", when used in this Chapter, refers to those issuers.

As mentioned in previous Chapters, Article 7 of the Transparency Directive mentions as the ones responsible for complying with the terms of the Directive, including its Article 4, which mandates the drawing up of financial and sustainability information, are the following persons: the issuer, its administrative, management or supervisory bodies, or the persons responsible within the issuer.

The definition of "issuer", recalling what has already been discussed in this Dissertation, is provided in Article 2(1), item (d), of the Transparency Directive, and means "*a natural person, or a legal entity governed by private or public law (…) whose securities are admitted to trading on a regulated market*". It is now important to define a term that has not been discussed in the Dissertation up to this moment: the "persons responsible within the issuer". This does not have a definition in the Transparency Directive and is only used two other times throughout its text, the first in Article 4(2), item (c), which deals with the preparation of annual financial reports, and the second in Article 5(2), item (c), which deals with the preparation of half-

annual financial reports. Given the similarity of wording of both texts, and the relevance of the annual financial report over the half-annual financial report, it is instrumental to the analysis of the meaning of this term the reproduction only of the text of Article 4(2), item (c), which follows:

> *"(…) persons responsible within the issuer, whose names and functions shall be clearly indicated (…) that, to the best of their knowledge, the financial statements prepared in accordance with the applicable set of accounting standards (…) and that the management report includes a fair review of the development and performance of the business (…) and, where appropriate, that it is prepared in accordance with sustainability reporting standards".*

In this sense, one may interpret that the "persons responsible within the issuer" for complying with the terms of the Transparency Directive mentioned in Article 7 are the same persons responsible for preparing the financial statements and management report, which, as discussed in the Chapter "3.1. Undertakings Subject to Articles 19a and 29a of the Accounting Directive", is a typical statutory duty of administrators of undertakings.

As also discussed in Chapter "3.1. Undertakings Subject to Articles 19a and 29a of the Accounting Directive", one must necessarily interpret "administrative, management or supervisory bodies" to reference the members of such bodies, and not the bodies themselves, since a basic assumption of legal responsibility is legal personality, which is not an attribute of these bodies, but only of their individual members, be them natural or legal persons. Furthermore, one may interpret Article 7 in conjunction with Article 28(2) of the Transparency Directive as a further argument in support of understanding this responsibility to be for the members of such bodies. This is because Article 28(2) makes explicit reference to "members" of administrative, management or supervisory bodies of an undertaking when addressing applicable sanctions for breaches of duties imposed by the Transparency Directive.

The civil nature of this responsibility, which damaged parties may argue when seeking reparations for damages suffered by them due to non-compliance with rules

regarding the preparation of financial or sustainability information, is the most relevant aspect to be analysed in this Dissertation. However, as per Article 28(1) of the Transparency Directive, which explicitly allows Member States to impose not only administrative measures and sanctions, but also criminal sanctions applicable to breaches of the rules set forth in that Directive, such responsibility may also undertake administrative and criminal meanings.

Even though the text of Article 7 of the Transparency Directive does not mention that the responsibility among members of administrative, management or supervisory bodies is “collective”, one may also imply it to be shared among such members due to the reference to the term “bodies”, which are usually comprised of more than one member, sometimes acting as a collegiate.

Finally, the greatest novelty introduced by the Transparency Directive is that, contrary to the Accounting Directive, it also includes the undertaking itself – more specifically, the issuer – as responsible for drawing up financial and sustainability information. The impacts of this inclusion will be discussed in the next Chapter of this Dissertation, “4. Liability for ESG Reporting Obligations: Possibility of an Insurance Coverage”.

Reprising the conclusions reached on the Chapter “3.1. Undertakings Subject to Articles 19a and 29a of the Accounting Directive”, the nature of the responsibility set forth in Article 7 of the Transparency Directive, is, therefore, primarily civil, with the possibility of also assuming administrative or criminal characteristics; that it is extra-contractual; that it is dependent on fault; and that it is shared among administrators found to be at fault, exempting administrators which have not acted on fault.

4. LIABILITY FOR ESG REPORTING OBLIGATIONS: POSSIBILITY OF AN INSURANCE COVERAGE

Now that the issue of understanding the nature of the responsibility for the drawing up and publishing of financial and sustainability information in the context of an undertaking's financial statements and management report has been solved in the previous Chapters, this Dissertation turns to its main research question, which is identifying the proper insurance coverage the persons legally responsible could purchase to protect themselves against the risk of non-compliance.

As discussed before, the persons responsible for preparing and publishing financial statements and a management report including sustainability information, as set forth in the Accounting Directive and in the Transparency Directive, depend on whether the undertaking about which the financial statements and management report are to be prepared belongs to one of the three following groups:

1. large undertakings, and small and medium-sized undertakings, except micro undertakings, which are public-interest entities, and parent undertakings of a large group;
2. large subsidiary undertakings, and small and medium-sized undertakings, except micro undertakings, which are public interest entities, that have an ultimate parent undertaking governed by the law of a third country, as well as a branch of an undertaking governed by the law of a third country that is either not part of a group or are ultimately held by an undertaking that is formed in accordance with the law of a third country; and
3. issuers whose securities are admitted to trading on a regulated market situated or operating within a Member State of the European Union.

The analysis conducted in the previous Chapters also identify the persons responsible for each of these groups, which are, respectively:

1. members of the administrative, management and supervisory bodies of the undertaking;

2. members of the administrative, management and supervisory bodies of the subsidiary undertaking of a parent undertaking governed by the law of a third country, or the persons indicated to manage or represent the branch office of a head office governed by the law of a third country, depending on whether the entity operating in a Member State is a subsidiary undertaking or a branch, respectively; and
3. members of the administrative, management or supervisory bodies of an issuer of securities admitted to trading on a regulated market situated or operating within a Member State of the European Union, and the issuer itself.

Finally, the previous Chapters also concluded that the responsibility in question, even though capable of being understood as having administrative or criminal implications, have primarily civil attributes, aiming at protecting third parties from damages suffered due to non-compliance with the rules set forth in the Accounting Directive and in the Transparency Directive. The specific rule in question – that of preparing financial and sustainability information and publishing it by means of drafting financial statements and a management report – is a statutory duty of administrators of a given undertaking, since it is a duty imposed by Law, and not contract, being, therefore, extra-contractual in nature. Understanding this duty as comprising strict responsibility – that is, responsibility irrespective of fault – has also been found to be the minority view of the literature. This Dissertation, for the reasons exposed in previous Chapters, adopts the majority view most coherent with the principles of general responsibility depending on fault. Lastly, the members of the administrative, management or supervisory bodies found to be at fault share responsibility among them for the damages caused to third parties. Exception is made to issuers of securities subject to the Accounting Directive, which may also be responsible, alongside members of their administrative, management or supervisory bodies.

In this sense, one now turns to the issue of considering that, given the fact that these persons have a responsibility for publishing financial statements and a

management report including sustainability information, there is a risk this duty is not performed, or is performed in an incomplete or erroneous way by those persons, who thus incur in non-compliance with the Accounting Directive or with the Transparency Directive.

The reason for this non-compliance may be either negligence, in which these persons fail "*to exercise the level of skill and care required in the performance of a professional activity*" (PAOLINI and NAMBISAN, 2014, p. 68), or, as briefly explored in Chapter "3.1. Undertakings Subject to Articles 19a and 29a of the Accounting Directive", the result of fraudulent behaviour, or deliberate or wilful misconduct.

Further details are given in the literature (PAOLINI and NAMBISAN, 2014, p. 144; RAMOS, 2010, 291) regarding the classification of negligence in the following categories: *culpa in contraendo* (in which the administrator acts with carelessness), *culpa in eligendo* (in which the administrator chooses inexperienced or incompetent persons to perform delegated activities), or *culpa in vigilando* (in which the demonstrator did not properly supervise, inspect or scrutinise the activities performed by persons with managerial powers). Negligent behaviour may also be understood as "*any actual or alleged breach of contract, breach of duty, breach of trust, act, neglect, error, omission, misstatement, or misleading statement*" (PAOLINI and NAMBISAN, 2014, p. 18) that causes damage to third parties.

Once acting or failing to act, when supposed to, in any of the abovementioned manners when performing their activities as administrators of an undertaking, these persons incur in fault, which then gives rise to liability: these persons may be deemed responsible to indemnify third parties for any damages suffered by them. These damages ought to represent a pecuniary loss to such third parties, and there must be a direct link between the act or omission from the administrators of the undertaking and the damaged caused to third parties.

Only if all of the above requirements are met – act or omission, culpability, damage and causation (PAOLINI and NAMBISAN, 2014, p. 146) – will the administrators be obliged to indemnify third parties for their losses.

This represents a risk for administrators: in the course of their activities, the chances they incur in liability may become higher the bigger and more complex are the structure and the activities performed by the undertaking. Once the risk is

materialized, and damage is caused to third parties, the assets owned by administrators may be used to pay for indemnities. The risk of incurring in liability is, therefore, a risk for administrators' assets.

Luckily, administrators may recourse to a financial product capable of protecting their assets against the risk of incurring in liability: a civil liability insurance contract, designed specifically for liability that administrators (often directors and officers) of an undertaking might incur when conducting their professional activities. This is known as a D&O Insurance, and its details will be further investigated in this Dissertation.

It is important, however, to first introduce the concept of an insurance contract and its purpose, to then discuss the elements of a general civil liability insurance coverage that are applicable to a D&O Insurance contract. Once equipped with this understanding, it will be possible to conduct the analysis of the D&O Insurance coverage per se, and how it relates to the risks associated with the preparation and publishing of financial and sustainability information.

4.1. GENERAL ASPECTS OF (CIVIL LIABILITY) INSURANCE CONTRACTS

An insurance contract is a contract in which one of the parties, the insurer, agrees to offer coverage (indemnification) for risks associated with the occurrence of a future and uncertain event that, if materialized, could cause damage to the other party, the insured, against the payment of a certain amount (premium) by the inured to the insurer (BASEDOW, 2016, p. 77; CLARKE, 2017, p. 5; RAMOS, 2010, p. 22; REGO, 2008, p. 56).

Central to the concept of insurance is that of risk, which is understood as a possibility of a certain event occurring, possibility being understood as a probability that is different form either complete improbability, or absolute certainty (BASEDOW, 2016, p. 77; REGO, 2008, p. 59; SILVA, 2007, p. 202). This possibility is then valued as being undesirable, or inconvenient (REGO, 2008, p. 64), causing an adverse impact on the insured's assets (RAMOS, 2010, p. 423; REGO, 2008, p. 66-67). Another element that is part of the insurance contract, and that distinguishes it from other activities such as bets or gambling, is that of the insurable interest: the

occurrence of the risk against which there is an insurance coverage must be effectively considered to cause an adverse impact on the insured person's assets (RAMOS, 2010, p. 424; REGO, 2008, p. 161-162; SILVA, 2007, p. 214).

Because the element of risk is so important to insurance, reference is made in the literature in the sense of considering the insurance contract to be a risk allocation, or transfer, mechanism (PAOLINI and NAMBISAN, 2014, p. 1; SILVA, 2007, p. 172), that is, the economic consequences of the risks that the insured person is subject to, if materialized, are allocated, or transferred, from the insured to the insurer, who is the person that actually bears these economic consequences.

In this sense, a civil liability insurance contract is a specific type of insurance contract in which the risk is defined as the liability of the insured person for damages caused to third parties, which they are obliged to indemnify (BASEDOW, 2016, p. 78; CLARKE, 2017, p. 5, 61; PAOLINI and NAMBISAN, 2014, p. 14; RAMOS, 2010, p. 425; REGO, 2008, p. 528). The purpose of this insurance is twofold: while protecting the assets of the insured against losses caused by the indemnifications they are obliged to pay to third parties, they also protect the interests of third parties themselves (SILVA, 2007, p. 103). The latter is especially true when considering that the majority of legal systems recognize to third parties the right to start a civil lawsuit to seek indemnification for their losses directly against the insurer, which confer to civil liability insurance contracts peculiar characteristics to be considered a strong device for promoting social welfare (BASEDOW, 2016, p. 301; SILVA, 2007, p. 108-109).

It is important to notice that, in this type of insurance contract (that of civil liability), the insurer is not considered the person who is liable for the damages caused to third parties. This liability remains with the insured: by means of the insurance contract, the insurer is under the obligation to indemnify the damaged third-party, but does not assume liability for the damages (SILVA, 2007, p. 156). The liability must also be defined in "*a judgment, an arbitration award or a binding settlement contract*" (PAOLINI and NAMBISAN, 2014, p. 3), the latter possible only with the insurer's consent (BASEDOW, 2016, p. 291).

It is of extreme importance for the purpose of this Dissertation to stress that, as mentioned previously, liability may arise from either negligent behaviour, or

fraudulent behaviour, or even deliberate or wilful misconduct. These two types of liability, that resulting from negligence and that resulting from fraud/deliberate or wilful misconduct, have different consequences when it comes to insurance coverage offered by civil liability insurance contracts.

The literature unanimously defends that only liability arising from negligence is covered by a civil liability insurance contract (BASEDOW, 2016, p. 289; PAOLINI and NAMBISAN, 2014, p. 16, 83). Liability arising from fraud, deliberate or wilful misconduct, or administrative liability (penalties) and criminal sanctions, are excluded from coverage (ABREU, 2013, p. 854; BASEDOW, 2016, p. 289-290; CLARKE, 2017, p. 17; MAGNUS, 2001, p. 201; PAOLINI and NAMBISAN, 2014, p. 17, 19, 68-69, 79, 80; RAMOS, 2010, p. 393). In this sense, the insured's assets are protected against indemnifications eventually due to damaged third parties only when the act or omission that resulted in liability is that of a negligent behaviour.

4.2. D&O INSURANCE

This Chapter has two purposes: the first is to understand what is a D&O Insurance contract and what are its main characteristics, that is, what distinguishes the coverage it offers to administrators of undertakings from other (civil liability) insurance contracts; and the second is to discuss whether risks associated with negligence in preparing and publishing financial and sustainability information are covered by this product of insurance.

The D&O Insurance contract is a civil liability insurance contract which covers, specifically, the liability risk of administrators – usually, directors and officers, hence the name "D&O" – of any given undertaking, while conducting their professional activities as administrators of such undertakings (RAMOS, 2010, p. 417). Because of this, the D&O Insurance is usually classified as a professional liability insurance contract (PAOLINI and NAMBISAN, 2014, p. 2, 68). Nonetheless, general aspects of a civil liability insurance contract discussed in the previous Chapter apply in its entirety to the D&O insurance, namely:

1. The D&O Insurance is an insurance contract in which one party, the insurer, agrees to offer coverage for liability risks

the insureds, administrators of a given undertaking, face when conducting their professional activities as administrators, against the payment of a premium. Other persons not necessarily members of administrative, management or supervisory bodies of undertakings, but that have important and prominent roles within the undertaking, may also be indicated as insureds in an insurance contract (RAMOS, 2010, p. 288-289). As seen below, the undertaking itself may also be added as an insured;

2. The liability risks covered by a D&O Insurance are those resulting from negligent behaviour from the insureds;
3. Liability must be confirmed by means of a judgement, an arbitration award, or by a binding settlement contract; and
4. Indemnity is paid directly to damaged third-parties, who usually have the right to seek indemnification directly from the insurer.

Specific characteristics of D&O Insurance contracts that differentiate them from other professional liability insurance contracts are the following features, which will be discussed in detail below: the structure of coverages, and the role of the undertaking in the insurance contract.

Usually, the D&O Insurance contract comprises three sets of coverages, denominated as Side A, Side B and Side C. Side A coverage is that offered towards liability for individual administrators; Side B coverage is that of the undertaking's own liability for payments it has done to indemnify its own administrators for their negligent conduct; and Side C, which is the coverage offered to undertakings for their own liability towards third parties (also called "entity" or "corporate" cover because of this). Side A and Side B coverages are considered as basic coverages for D&O Insurance coverages, while Side C is offered as an additional coverage in some contracts (PAOLINI and NAMBISAN, 2014, p. 60; RAMOS, 2010, p. 264-265, 267).

With regards to the role of the undertaking, it is important to notice that the company is usually the one that purchases the insurance contract in favour of its own administrators (ABREU, 2013, p. 851; RAMOS, 2010, p. 289), taking the role of the policyholder. The policyholder is not necessarily an insured: their assets are not necessarily covered against liability risks for damages caused to third parties in the insurance policy. However, as seen above, the undertaking itself might be included as an insured party, by means of including Side C coverage to the insurance contract.

The role of the undertaking gives rise to some concerns, which will be now discussed. If not included in the insurance contract as an insured, but merely as a policyholder, the undertaking is considered, for liability purposes, as a third party, capable of suffering damages from negligent behaviour from its own administrators, and, thus, being capable of triggering coverage, as a third party, for these damages (RAMOS, 2010, p. 421; REGO, 2008, p. 532). However, if included in the insurance contract as an insured by means of a Side C coverage, for instance, the literature notes that insured vs. insured claims – that is, claims for compensation made by an insured towards another insured of the same contact – are often excluded from coverage in D&O Insurance contracts (PAOLINI and NAMBISAN, 2014, p. 72-76). In this sense, claims brought forward by the undertaking against its own administrators, or vice-versa, might not be covered under a D&O Insurance, if they are all insureds under that insurance contract.

Another feature of a D&O Insurance policy is its composite nature, that is, the insurable interest is considered to be separable: the insurable interest of each individual insured – administrator and the undertaking itself, if coverage has also been extended to the latter – are to be deemed as separate, in the sense that "*each composite insured has a separate claim against the insurer and the insurer for its part may have separate defences against the insureds*" (PAOLINI and NAMBISAN, 2014, p. 61). The consequence for this is that if coverage is not applicable to one insured, this does not mean that it is not applicable to all other insureds as well.

Of particular interest to this Dissertation, and aiming at answering its main research question defined in the Chapter "1. Introduction", is the analysis of whether negligence in drawing up financial and sustainability information may be covered in

the scope of a D&O Insurance contract. The majority view of the literature, as discussed below, is that this is a typical case of liability covered under the general terms of the D&O Insurance.

Firstly, the literature extensively cites the duty to draft financial statements and its accompanying management report as a statutory duty of administrators, designed especially for the protection of interests of shareholders and third parties (ABREU, 2013, p. 907-908; RAMOS, 2010, p. 142-143). Consequently, administrators are unequivocally liable towards third parties for errors in the financial statements and management report (RAMOS, 2010, p. 140).

Secondly, the literature also exemplifies how the breach of such duty has already been deemed, in the context of judicial proceedings which concerned losses suffered by shareholders due to inflated prices of stocks caused by unrealistic financial statements, a valid cause for liability that was eventually covered under the terms of a D&O Insurance (PAOLINI and NAMBISAN, 2014, p. 32-35).

It is important to notice, however, that the literature does not mention coverage for errors in sustainability information conveyed in financial statements and management reports of undertakings, especially when considering that this is an absolute novelty in the legal landscape of the European Union, with very recent developments. Some pieces of legislation that have been published in the Official Journal of the European Union, for instance, have yet to become applicable, and their consequences in the real word have yet to be felt.

However, given the understanding, as mentioned in the Chapter “2.3. CSRD”, that sustainability information has become comparable to financial information in relevance and importance, and that it has become an integral part of the management report which undertakings ought to produce under the terms of the Accounting Directive and the Transparency Directive, one could argue that failure to correctly prepare and publish sustainability information could be understood as comparable to failure to correctly prepare and publish a financial statement with financial information, and a breach of compliance with the rules regarding how a management report shall be drawn up. In this sense, a breach to correctly convey sustainability information in a management report, in the terms of legislation enacted

by the European Union regarding how this information shall be conveyed, may also be covered under the general terms of a D&O Insurance.

Given the conclusion reached above, and returning to the responsibilities identified in the course of this Dissertation, one is now fully equipped to answer the main research question proposed at the beginning of this discussion: a D&O insurance policy is capable of offering the adequate insurance coverage for liability risks associated with the drawing up of sustainability information faced by the following persons in the course of their professional activities:

1. members of the administrative, management and supervisory bodies an undertaking, included as insured parties to a D&O Insurance contract;
2. members of the administrative, management and supervisory bodies of the subsidiary undertaking of a parent undertaking governed by the law of a third country, included as insured parties to a D&O Insurance contract, or the persons indicated to manage or represent the branch office of a head office governed by the law of a third country, given that the persons indicated to manage or represent the branch office are duly included as insured parties in the D&O Insurance due to the importance and prominent role they play in the branch office, depending on whether the entity operating in a Member State of the European Union is a subsidiary undertaking or a branch, respectively; and
3. members of the administrative, management or supervisory bodies of an issuer of securities admitted to trading on a regulated market situated or operating within a Member State, included as insured parties to a D&O Insurance contract, and the issuer itself, if also included as an insured party by means of the additional Side C coverage of a D&O Insurance.

As observed above, an already existing type of insurance contract – that of the D&O Insurance – is capable of offering specific coverage for risks associated with ESG reporting obligations imposed by recent legislative developments in the European Union, once the necessary adjustments in the wording of the policy, or a more encompassing interpretation of it, are applied. In this sense, a completely new, “ESG-Insurance” policy is rendered unnecessary, thus answering the last two of the most relevant research questions proposed in the “1. Introduction” section of this Dissertation.

5. CONCLUSIONS

ESG – Environmental, Social and Governance topics are here to stay. In view of increasing preoccupations with how undertakings operating in the economy affect the sustainability of our environment and our society, as well as how environmental and societal concerns may impact the performance of such undertakings, the legal rules concerning access of information and transparency of businesses have made it mandatory for undertakings to disclose to their stakeholders how they are dealing with sustainability issues.

Perhaps almost as important as the duty to disclosure these sorts of information, is the question of how this information ought to be disclosed. This is because a lack of standardization may lead to distrust among the public regarding the importance of sustainability issues, as well as hinder the ability of comparing the performance of different undertakings, each adopting different rules and methodologies.

The European Union has been at the forefront in the effort of setting a regulatory standard when it comes to ESG and sustainability information. The first part of this Dissertation aimed at showing exactly that.

However, with new duties being imposed to undertakings and their administrators as to how they should disclose sustainability information in their financial statements and management report, often very intricate and detailed in nature, while also being new and thus preventing them from relying on experience, brings forth a considerable risk of non-compliance with these rules, and, ultimately, of being held liable for damages caused to third parties because of their negligent non-compliance.

The ultimate purpose of this Dissertation was, then, to understand if contracting an insurance coverage currently offered in the market could be a risk management tool to help these undertakings and their administrators to properly allocate these risks. After carefully analysing the responsibilities derived from the newly introduced sustainability information disclosure rules in the European Union and understanding the nature of the risks they encompass, the main conclusion is that the D&O Insurance may be an excellent tool for undertakings and their

administrators not only to better deal with the risks of their activities, but also to guarantee that there is a mechanism in place that guarantees that occasional damages caused to third parties would not be left unrepaired.

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