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EXECUTIVE DEBRIEF

NAVIGATING THE EVOLVING LANDSCAPE OF CORPORATE GOVERNANCE

An initiative of the ECGI Patrons Council

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CHATHAM HOUSE RULE

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EXECUTIVE SUMMARY

The inaugural ECGI (European Corporate Governance Institute) Patrons Council Meeting in March 2025 convened senior leaders and experts to discuss the evolving corporate governance landscape amid geo-economic fragmentation, regulatory pressures, and shifting investor priorities. Discussions emphasised the growing political influence on corporate governance and the need for firms to navigate these complexities strategically.

One major theme was the increasing need for defensive mechanisms against politically motivated investor decisions and regulation. The U.S. approach to responsible investment, corporate governance and regulatory oversight increasingly diverges from other OECD countries, including anti-bribery conventions and climate goals. This is increasingly reflected in the stance of U.S. pension funds, that represent just under half of worldwide pension assets.

The attitudes of asset managers, service providers and private equity firms are changing even more rapidly. Hedge fund activists feel emboldened to launch campaigns that run counter to declared corporate responsibility objectives. These developments raise fundamental questions about the ownership and control of European companies. Do European firms need stronger safeguards, such as golden shares, dual-class structures, or state-backed investment funds, to counteract politicised voting trends and regulatory retaliation? The role of sovereign wealth funds in corporate governance was also debated.

Another key issue was balancing regulatory ambition with economic competitiveness. The Corporate Sustainability Due Diligence Directive (CSDDD) has geopolitical and competitive implications, raising concerns that excessive regulation could weaken European industry. Boards do not have the bandwidth to deal with the increased complexity of regulation alongside the complexity of running a business, so it gets dealt with at lower levels in the organisation. While some firms are well-prepared, others fear de-industrialisation and retaliatory trade measures from non-EU markets, particularly the U.S. There are distinct regional blocs of regulation, making it difficult for companies to identify which rules they need to comply with. This fragmentation also makes it challenging to anticipate future regulatory changes.

Discussions on shareholder stewardship and corporate control highlighted the rise of customised voting strategies and pass-through voting. In theory, customised voting policies provide more opportunity to align the stance of asset managers with the wishes of asset owners. In practice, while pass-through voting would allow end investors to directly influence voting decisions, it remains largely theoretical rather than operational. The standard voting policies of the major proxy advisers continue to dominate actual voting practices. Concerns over executive compensation constraints in Europe and a widening transatlantic divide on ESG priorities further underlined governance challenges.
Ultimately, the meeting emphasised that boards must anticipate regulatory shifts, geopolitical tensions, and investor dynamics. Companies should proactively engage with regulators and investors to ensure governance frameworks support both sustainability and global competitiveness. As governance becomes increasingly politicised and fragmented, firms must develop adaptive strategies to maintain strategic autonomy while meeting evolving stakeholder expectations.

SESSION 1: NAVIGATING THE CSDDD

The first session of the ECGI Patrons Council explored the evolving regulatory landscape, focusing on the Corporate Sustainability Due Diligence Directive (CSDDD) and its implications for corporate governance, compliance, and competitiveness.

1. CSDDD: The Most Ambitious ESG Legislation to Date

- CSDDD is considered "the most ambitious piece of ESG legislation hitherto promulgated."
- Unlike the OECD Due Diligence Guidance, which is a set of recommendations, CSDDD is mandatory.
- Non-compliance leads to sanctions, whereas failure to follow OECD guidance primarily results in reputational risks.
- The directive requires in-scope companies (large EU firms and non-EU firms with significant EU market presence) to:
  - Identify, prevent, mitigate, and account for adverse human rights and environmental effects.
  - Extend due diligence checks across subsidiaries and business partners in the value chain.
  - Adopt and implement a climate transition plan aligned with the Paris Agreement to achieve climate neutrality by 2050.
- Process vs. Outcome: The directive focuses on "appropriate measures" rather than guaranteeing specific results, which may be necessary but possibly insufficient to dispel concerns about hindsight bias in enforcement.

2. "Attack from Within" – Proposed Amendments to Weaken CSDDD

- Political divisions within the EU have led to attempts to water down the directive, with proposals (omnibus / simplification measures) to:
  - Narrow the scope of due diligence for indirect business partners.
  - Increase monitoring intervals and reduce compliance burdens.
  - Remove the mandatory termination of non-compliant business relationships.
  - De-harmonise penalties at the national level, removing the prospect of NGO or trade union litigation.
  - Delay implementation by one year.
- Some participants expressed concern that these amendments could weaken the directive's impact, while others viewed them as necessary adjustments to avoid excessive burdens on businesses.

3. "The Enemy from Without" – U.S. Resistance & Extraterritorial Implications

- The Brussels Effect: CSDDD is expected to impact large U.S. companies operating in the EU, similar to GDPR.
- It extends to international human rights and environmental conventions that the U.S. has not ratified, potentially causing compliance conflicts.
- Political backlash in the U.S.: Some state-level regulations discourage or even prohibit companies from adopting climate-related policies. A U.S. senator introduced a bill to prevent American firms in key industries (e.g., defence, rare minerals) from complying with foreign sustainability rules.
- The Caremark Doctrine (Delaware corporate law) may ironically require U.S. firms to take CSDDD compliance more seriously than some European firms, due to the higher legal risks of failing to oversee ESG-related risks.
- Participants raised concerns that EU sustainability rules could trigger retaliatory measures in trade policy, potentially affecting European firms doing business in the U.S..

4. Business Concerns: Competitiveness, Investment Risks, and Compliance Challenges

- Some participants warned that over-regulation could accelerate de-industrialisation, pushing industries like steel, chemicals, and automotive outside of Europe (e.g. towards China).
- Participants highlighted the complexity of implementing CSDDD, especially in global supply chains.
- Concerns over regulatory fragmentation: Different jurisdictions are adopting conflicting rules, making compliance a challenge for multinational firms. Regulatory divergence can lead to sustainability laws interacting unpredictably with antitrust, investment, and trade policies.
- Several business representatives highlighted the risk of Europe becoming ‘uninvestable’ due to excessive regulatory burdens, particularly in energy-intensive industries like steel, chemicals, and automotive.
- Some firms that have already implemented robust sustainability reporting feel better prepared for compliance, while others—particularly SMEs—struggle with the high costs and complex requirements.
- There was widespread concern about the lack of a level playing field, with Europe adopting stricter rules than its global competitors.

5. The Role of Corporate Governance and Boards

- Boards must take a proactive role in navigating CSDDD and its geopolitical implications.
- Some attendees suggested strengthening corporate diplomatic expertise to engage more effectively with policymakers.
- There was agreement that companies should coordinate strategically to advocate for pragmatic regulatory frameworks, ensuring that sustainability and competitiveness go hand in hand.

The session highlighted that sustainability regulation is no longer just a compliance issue—it is a geopolitical and competitive challenge. While some firms are well-prepared, others face significant adaptation costs. Participants emphasised the need for greater industry coordination and proactive engagement with regulators to strike a balance between sustainability goals and economic competitiveness.

SESSION 2: STEWARDSHIP PRIORITIES AND EXPECTATIONS

The second session of the ECGI Patrons Council explored the evolving stewardship priorities of investors, the shifting regulatory environment, and the growing tensions between global markets over corporate governance expectations.

1. The Expanding Scope of Investor Expectations

- Investors are increasingly setting broad, long-term expectations for companies, covering both traditional corporate governance issues and material environmental and social risks.
- Voting remains a support mechanism rather than a punitive tool:
  - 95% of votes are cast in line with management.
  - 70% of all meeting votes align with board recommendations on all items.
  - However, voting is not typically used as a tool to push best practices—investors prefer engagement over coercion.
- Some investors now pre-disclose voting intentions five days before AGMs, allowing companies and stakeholders to anticipate decisions.

2. U.S.-Europe Divergence on Shareholder Engagement

- Recent regulatory changes in the U.S. are making shareholder engagement more difficult.
- New disclosure rules (5% ownership threshold) mean that certain investors can no longer engage with companies as freely without triggering complex disclosure requirements.
- This has had a chilling effect on investor-company engagement, particularly in executive compensation discussions and governance reforms.
- Some fear that the new U.S. rules will push investors to prioritize short-term financial returns over long-term sustainability strategies.

3. ESG, Political Backlash, and Shifting Investment Strategies

- The session touched on the political polarisation of ESG:
  - Some U.S. states are actively discouraging ESG integration, while in Europe, sustainability expectations remain deeply embedded.
  - Participants noted that Europe could gain a competitive advantage as U.S. investors retreat from ESG-focused investments.
- A notable case study was the lawsuit against Follow This and Exxon, which raised concerns about the limits of shareholder rights in promoting ESG issues.

- The rise of activist investors was discussed:
  - Activist campaigns are not always aligned with long-term corporate survival.
  - Some participants shared concerns about activists securing board seats and driving strategic decisions misaligned with the company's goals (e.g. anti-ESG activists) whilst others saw activists as a force that could contribute to speeding up changes, i.e. something positive.

4. Private Equity and the Future of Corporate Influence

- Private equity is increasingly shaping governance trends, particularly in industries like energy and defence, where public scrutiny is high.
- A growing bifurcation is emerging between public and private markets:
  - U.S. pension funds are moving away from ESG-driven strategies and focusing solely on returns.
  - This could result in more controversial sectors (e.g., fossil fuels, defence) shifting into private markets, where disclosure requirements are lower.
- $1.5 trillion in dry powder (uninvested capital) is waiting to be deployed by private equity funds, raising concerns about the governance and transparency of firms turning to private markets, particularly in industries like energy and defence where public scrutiny is high. We need to scale up private venture capital in Europe and have a different attitude towards incentives for such asset managers.

5. The Rising Influence of Sovereign Wealth Funds and State-Controlled Investment

- The discussion highlighted the growing influence of sovereign wealth funds (SWFs), particularly in Europe and Asia.
- President Trump has advocated for a US Sovereign Wealth Fund.
- A key question was raised:
  Do European economies need their own "sovereign wealth bazooka" to compete with state-backed investment funds from the U.S. and China?
- Some participants warned that if private capital becomes too politically driven, Europe may need stronger intervention mechanisms to maintain competitive independence.

SESSION 3: VOTING TRENDS

The third session of the ECGI Patrons Council explored voting trends, custom voting policies, and the emerging influence of pass-through voting on corporate governance. The discussion underscored the complexity of shareholder decision-making, the shifting influence of proxy advisors, and the growing divide between European and U.S. approaches to corporate governance.

1. The Evolution of Custom Voting Policies

- Custom voting policies are now the norm among large institutional investors.
  - In 2021, 91% of institutional votes were based on custom policies, increasing to 94% by 2023.
  - This shift undermines the long-held assumption that investors blindly follow ISS or Glass Lewis recommendations.
- Custom voting policies are increasing investor independence, but regional pay constraints remain a concern for European companies.
- Some investors now engage year-round with proxy advisors, rather than only during proxy season.
- There was discussion about whether proxy advisors (like ISS and Glass Lewis) should be seen as governance "kingmakers" or merely one of many influencing factors.

2. European vs. U.S. Pay Practices: The Transatlantic Gap

- Concerns about European executive compensation competitiveness were raised:
  - The UK’s pay-for-performance gap with U.S. firms is widening, leading to concerns about attracting and retaining top talent.
  - Some European companies are considering reincorporating in the U.S. if compensation restrictions persist.
- The stance of proxy advisers on peer group selection was criticised:
  - European boards want more flexibility to compare themselves with U.S. firms, but ISS and Glass Lewis push for regional comparisons.
  - This has led to frustration among UK-listed firms competing for international talent.
- 10% of FTSE 350 companies proposed remuneration policy updates, and close to 30% sought increases in short-term (STI) or long-term (LTI) executive pay.
- Time-based awards (hybrid plans) are increasing in the UK, with an expectation of stronger justifications from boards.
- Over 95% of director election votes in EMEA received support, and remuneration reports saw over 90% approval, though dissent was higher where salary increases or poor investor engagement occurred.

3. The Rise of Pass-Through Voting: Who Really Holds the Power?

- Pass-through voting is gaining traction but remains in early stages:
  - BlackRock, Vanguard, and State Street now offer it, allowing fund investors to choose from preset voting policies rather than delegating votes to the asset manager.
  - However, current uptake remains low (around 5%), raising concerns about quorum issues and greater activist investor influence.
- Whilst proxy advisers have enabled aggregation of individual voting preferences into coherent blocs, the emergence of pass-through voting suggests a move back towards fragmentation of voting behaviour.
- Some questioned whether pass-through voting is a defensive move by asset managers: *"Are BlackRock and Vanguard using pass-through voting to distance themselves from governance decisions and avoid political scrutiny?"*
- Key statistics from 2024:
  - $3.1 trillion out of $6.3 trillion in index assets are eligible for pass-through voting.
  - $679.3 billion worth of assets exercised voting choice, with $285.5 billion newly committed.
  - 40,000 investors (about 2% of those eligible) participated in pass-through voting during the 2024 proxy season.
  - The most frequently chosen voting policies were:
    - Company Board-Aligned Policy
    - Vanguard Advised Funds Policy
  - A notable addition to ISS voting policies is Bowyer Research, the most conservative policy, potentially aligned with the U.S. Administration.
- There are legal challenges:
  - U.S. law currently does not allow asset managers to split votes—funds must vote all shares under one policy, making true pass-through voting impractical.
- The long-term impact of pass-through voting is still uncertain, with concerns over engagement, quorum, and activist influence.

4. Voting Rationality vs. Political Voting

- A shift from financially rational voting to politically motivated voting is emerging, particularly in the U.S.:
  - Some red-state pension funds are rejecting ESG proposals, even when they align with long-term financial returns.
  - This raises concerns about whether political pressures are distorting corporate governance decisions.

- There was debate over whether Europe needs a stronger defensive mechanism:
    - Some participants suggested reintroducing golden shares or promoting the use of dual-class structures to counterbalance politically motivated voting trends.

5. The Role of Abstentions and Withheld Votes

- Traditionally, investors used abstentions to signal concerns without outright opposition.
- However, abstentions are declining, with voting becoming increasingly binary:
    - Some long-term investors worry that binary voting (for/against) reduces engagement incentives.
    - The question was raised:

"Should institutional investors return to using abstentions as a strategic tool in governance?"

The session ended with a call for deeper engagement between companies, proxy advisors, and regulators to ensure governance remains financially driven rather than politically influenced.

CONCLUDING REMARKS AND NEXT STEPS

- The final session brought together key themes from across the day, highlighting the need for strategic, forward-looking governance that reflects the realities of regulatory fragmentation, political polarisation, and shifting capital dynamics.
- Boards were encouraged to integrate policy foresight, geopolitical awareness, and investor engagement into their decision-making.
- It was the general view that organisations should maintain strategic independence despite current U.S. policy pressures, while acknowledging the importance of enhanced preparedness for rapid and adaptive responses. Corporate governance frameworks should balance necessary oversight with sufficient flexibility to enable timely adjustments in the face of evolving geopolitical challenges.
- Participants discussed the need for stronger industry coordination and new mechanisms to safeguard long-term value in an increasingly contested governance space.

Before concluding the meeting, a proposal was introduced to convene a Brussels-based forum in Autumn 2025, aiming to deepen engagement between business leaders and European policymakers. The envisioned two-day event would serve as a two-way platform for strategic dialogue, focusing not only on current regulatory challenges but also on long-term geopolitical and economic priorities.

EUROPEAN CORPORATE GOVERNANCE INSTITUTE

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