Commonwealth Climate and Law Initiative

Nature-related risks and Duties of Company Directors

Directors around the world generally have two core duties under national company laws: to exercise **care and diligence**, and **loyalty (promoting the success of their company)**. These duties are exercised in strategic planning, oversight of risk management, and attesting to the accuracy of disclosures and financial reporting. The law commonly **assesses the standard of directors' care and loyalty by reference to the evolving market, social, regulatory and legal context.** Company directors that do not appropriately consider nature-related risks may face **personal consequences for breaching their duties**.

Nature-related physical, transition and legal risks arise from a company's dependencies and impacts on nature and are increasingly understood to be **material to the short- and long-term success of individual companies** and to the global economy. The World Economic Forum's research in 2020 concluded that "$44 trillion of economic value generation—over half the world's total GDP—is moderately or highly dependent on nature and its services." In 2022 the CCLI reported that nature-related risks are likely to be relevant to directors' duties under a number of company law frameworks. This is evidenced by **independent and authoritative legal opinions written by acclaimed company and financial law barristers** in Australia, the UK and New Zealand. These opinions **clarify existing company law in their respective countries,** taking account of **comprehensive evidence** of recent global developments in:

- scientific understanding of global nature decline; and
- financial and economic understanding of risks arising from nature-related issues for companies, lenders, investors and wider financial systems.

These legal opinions do not make new law or advocate for changes in the law, but clarify existing legal duties. Nature-related risks fall within existing financial risk categories and are not new categories of risk.

The relevance of nature-related risks to directors' duties is partly jurisdiction and location specific, but there are sufficient commonalities between the laws of different countries that many conclusions of the UK and the Australia opinions may be applicable to other countries. (See for example Canada, India, South Africa, Singapore, Hong Kong and Malaysia.)

In some circumstances, directors may need to consider material nature-related risks in both financial and non-financial reporting, under existing national regulations.

What are the risks for board directors?

It is important to note that even in the absence of disclosure regulations, directors will still need to consider and manage material nature-related risks if they are to comply with their duties of care and loyalty.

Directors could potentially breach their duties by failing to consider or act on relevant nature-related risks. A director can face significant consequences for breach of duty, including claims for damages, termination of their position, adverse reputational consequences and challenge to executive directors' remuneration and 'bad leaver' provisions.

False statements about a company's consideration of nature-related issues (greenwashing) could expose the company and its directors to:

- latent financial risks arising from unaddressed nature-related impacts and dependencies;
- the risk of shareholder and investor claims (including for fraud); and
- reputational risk.

What are the opportunities for directors?

The UK legal opinion provides a **five step roadmap** for directors to use to address nature-related risks and steer their company competitively through the nature-positive transition.

1. **Identification:** Directors who actively consider the extent to which their company faces nature-related risks will find it easier to make commercial decisions and justify action or inaction.
2. **Assessment/evaluation**: Directors can assess which risks are relevant and non-trivial and evaluate their potential to cause harm to the company, aided by TNFD guidance and materiality assessments.
3. **Risk management/mitigation:** Consider how best to manage and/or mitigate relevant and non-trivial risks where appropriate, for example through a risk management framework.
4. **Disclosure:** Decide i) what is required to be disclosed under applicable laws and ii) whether to voluntarily disclose (in response to market or investor expectations) material nature-related risks or impacts.
5. **Documentation:** By properly recording how they have taken the above four steps in board minutes, agendas, memoranda, and reports, directors can protect themselves from litigation and legal risks.