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# DUTIES AND RESPONSIBILITIES OF DIRECTORS OF JOINT STOCK COMPANIES ON CORPORATE SOCIAL RESPONSIBILITY: AN EVALUATION WITH RESPECT TO TURKISH COMPANY LAW

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## Abstract

Company law regulations establish the responsibility of directors towards the company and its shareholders (and to creditors in case of insolvency). The interests of stakeholder groups, including the interests of employees, the environment and the society considered as irrelevant in terms of company law. Because directors' responsibilities defined by company law disregard social responsibilities, board of directors and managers cannot enjoy a complete discretion in respect to Environmental-Social-Governance (ESG)-related issues. In the literature, the subject of companies engaging socially responsible conduct mainly addressed by the virtue of business ethics and many of the discussion disregarded the role of company law on the matter. This paper is aimed to identify the roles and responsibilities of directors under Turkish Commercial Code with respect to corporate social responsibility and specify the conditions for the validity of their decisions on socially responsible conduct.

## Key Words

Corporate Entity Theories • Corporate Social Responsibility • Turkish Commercial Code • Business Judgment Rule • Environmental-Social-Governance (ESG)

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# ANONİM ŞİRKET YÖNETİCİLERİNİN KURUMSAL SOSYAL SORUMLULUK İLE İLGİLİ GÖREV VE SORUMLULUKLARI: TÜRK ŞİRKETLER HUKUKU AÇISINDAN BİR DEĞERLENDİRME

## Öz

Şirketler hukuku mevzuatı, yöneticilerin sorumluluğunu şirkete ve pay sahiplerine (ve iflas durumunda alacaklılara) karşı düzenlemiştir. Çalışanların, çevrenin ve toplumun çıkarları dahil olmak üzere diğer menfaat sahibi grupların çıkarlarının şirketler hukuku açısından konu dışı olduğu düşünülmektedir. Yöneticilerin şirketler hukukunda tanımlanan yasal yükümlülükleri, diğer sosyal sorumlulukları göz ardı ettiğinden, yönetim kurulunun ve yöneticilerin Çevre-Sosyal-Kurumsal Yönetim (ÇSY) ile ilgili konulardaki takdir yetkileri sınırsız değildir. Literatürde, sosyal açıdan sorumlu davranışlara dahil olan şirketler, daha çok iş etiği kapsamında ele alınmış ve tartışmaların çoğu bu konuda şirketler hukukunun rolünü göz ardı etmiştir. Bu makale, yöneticilerin Türk Ticaret Kanunu kapsamında kurumsal sosyal sorumluluğa ilişkin rol ve sorumluluklarının sınırlarını belirlemeyi ve sosyal sorumlu davranışa ilişkin kararlarının geçerlilik koşullarını ortaya koymayı amaçlamaktadır.

## Anahtar Kelimeler

Şirket Teorileri • Kurumsal Sosyal Sorumluluk • Türk Ticaret Kanunu • Ticari Takdir İlkesi • Çevresel-Sosyal-Kurumsal Yönetim (ÇSY)

## INTRODUCTION

In 2012, following the conference on Sustainable Development in Rio, the United Nations called upon "…*the private sector to engage in responsible business practices...*" and such an "…*active participation of the private sector can contribute to the achievement of sustainable development*".[1] As promoted by the United Nations Global Compact, responsible business practices include but not limited to supporting and respecting internationally accepted human rights, elimination of discrimination of labor, supporting initiatives to overcome environmental challenges through the development of environmentally friendly technologies.[2]

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1 Resolution adopted by the General Assembly on 27 July 2012 A/RES/66/288. The Future We Want, para. 46. https://www.un.org/ga/search/view_doc.asp?symbol=A/RES/66/288&Lang=E Accessed 27.01.2021.

2 Ten Principles of the UN Global Compact available at https://www.unglobalcompact.org/what-is-gc/mission/principles Accessed 27.01.2021.

Under one-tier corporate governance system, the board of directors is the single body entitled to govern and represent the company in all matters related to the management of the company, except for the roles and duties reserved to the general assembly. According to the Turkish Commercial Code (hereafter, TCC) the board of directors is authorized to make decisions on any actions and transactions required in order to conduct the business subject-matter of the company (TCC, art. 374). The roles of the management of the company at the highest level and giving instructions about these policies are assigned by law to the board of directors (TCC, art. 375). The management of the company at highest level is one of the non-transferable and indispensable duties of the board (TCC, art. 345). The board of directors is also responsible for the disclosure of corporate governance report.

Turkish company law has established the legal responsibility of managers towards the company and its shareholders, and to creditors in case of insolvency (TCC, art. 553/1).[3] On this ground, directors and managers are legally obliged to pursue the best interests of the company. Regarding the social responsibility of companies, the law has not issued any duty or responsibility for managers. Under the Turkish company law there are no specific provisions with respect to the duties and responsibilities of companies towards the interests of non-shareholder stakeholders, including the society and the environment. External laws and regulations, such as Labor Law No. 4857 governs the protection of the company's employees at the workplace. Similarly, the protection of environment (including biological, physical, social, economic, and cultural) is ensured by the Environmental Law No. 2872 in line with the principles of sustainable

[3] Within the scope of article 553 of the TCC, managers include persons who make decisions on behalf of the company and execute it, thus fulfilling the duties assigned to them for the realization of the company's field of activity. In this paper, "director" and "manager" are used interchangeably and they refer to the persons within the scope of article 553 but with different titles such as general manager, assistant general managers, senior managers, third parties appointed with management such as CEOs (under art. 369), executive committee or general coordinator. For description of the concept of 'directors', see YANLI, Veliye, "Şirkete Verilen Zarar Sebebiyle Sorumluluk Bağlamında "Yönetici" Kavramı ve Genel Kurul Kararı Gerekliliği Sorunu", Terazi Hukuk Dergisi, 14 (151), 2019, 46-57, p. 53.

development. As for company law, the two main duties imposed by law on the members of the board and third parties assigned with managerial responsibilities are the duty of care and the duty of loyalty.

The aim of this paper is to identify the role of directors for socially responsible business conduct. For that purpose, this paper firstly questions the roles and responsibilities of directors imposed by Turkish company law. This part will demonstrate directors' role for socially responsible companies in the light of the long-standing debate on the duty of directors towards shareholders versus larger stakeholders. Secondly, it discusses the legal capacity of directors in terms of considering ESG-related issues. Lastly, this paper will conclude by specifying the conditions to the validity of directors' discretion on socially responsible conduct under the business judgement rule.

## I. STATUTORY DUTIES OF DIRECTORS TO THE COMPANY

According to the Turkish company law, the members of the board and other third parties appointed with management are required to perform their duties with the care of a cautious manager and while fulfilling their duties they have to consider the best interests of the company (TCC, art. 369). Board members and managers are expected to follow general principles of law, i.e., acting in good faith (bona fide) while making business decisions. In other words, managerial decisions will be reviewed on an objective standard whether the company benefit is pursued in good faith while the manager performing his/her duties. When assessing the director's duty of care and the duty of loyalty the prominent question is whether a benefit was pursued in the interest of the company. A reasonable belief based on appropriate information that the directors were acting in the best interest of the company will set the standards.

At this point, unsurprisingly more questions arise. What does define (or should define) a company's interests? And who to determine those interests? The answers to these questions would differ according to the two predominant views put forward on the theories of the corporate

entity. One of those theories views the corporation as a "nexus of contracts"[4] and treats shareholders as the owners of the corporation.[5] Under this theory, the corporation is recognized as a "legal fiction" that is a separate legal entity independent from its founders. Even though the corporation has its own rights and properties under this separate legal personality, this theory still argues that the shareholders' interests should be centered because they invest their capital in the company to pursue particular economic interests.[6] Under this phenomenon the corporation is not seen fully independent from its owners especially in terms of its economic purpose. For that reason, the "nexus of contracts theory" accepts that the corporation is obliged to serve the interests of its shareholders.[7] This theory largely reflects the shareholder primacy view in which the corporate performance and shareholder value maximization are the substance for the purpose of the corporation.[8] The other predominant view on the theory of the corporation views the corporation as a concession from the state.[9] This group also sees the corporation as a legal fiction and an independent entity itself. According to this view, it is argued that the state grants corporations the legal entity status as a concession and thus the state should have a right to control over corporations and be able to define their purpose.[10] The advocates of this group accept non-shareholder groups as the

4 EASTERBROOK, Frank H. / FISCHEL, Daniel R., "The Corporate Contract", Columbia Law Review 89 (7), 1989, 1416-1448, p. 1418.

5 JENSEN, Michael C. / MECKLING, William H., "Theory of the Firm: Managerial Behavior, Agency Costs, and Ownership Structure", Journal of Financial Economies, 3, 1976, 305-360, p. 308-309.

6 ATTENBOROUGH, Daniel, "Giving Purpose to the Corporate Purpose Debate: An Equitable Maximization and Viability Principle", Legal Studies, 32 (1), 2012, 4-34.

7 MILLON, David, "Theories of the Corporation", Duke Law Journal, 1990, 201-262, p. 229-231; BRATTON, William W., "The New Economic Theory of the Firm: Critical Perspectives from History", Stanford Law Review 41, 1989, 1471-1527.

8 SMITH, D. Gordon, "The Shareholder Primacy Norm", The Journal of Corporation Law 23, 1998, 277-323.

9 MILLON (1990) p. 227.

10 BRATTON (1989) p.1502–1508.

legitimate contributors to the corporation and refer them as "stakeholders".[11]

Today, many businesses are organized under a corporate entity, so that they can channel small capitals to use them for the purposes of the business, and they have only been able to do this because of their legal personality status granted by the state. The law, in particular company law grants companies a legal personality to fulfill a specific economic purpose.[12] The capacity to have rights and obligations of joint stock companies includes all rights and obligations except for those based on human qualities such as gender, age, and kinship (TTC, art. 125).[13] Under this legal entity, a company can take legal action on its own, acquire or sell properties. The distinguishing feature of companies is that they have a separate and independent personality from their founders.[14] Companies exist independently of their founders, that is to say even if the founders or shareholders die or sell their shares to others, the continuity of the company will not be affected.[15] Although the shareholder value approach accepts shareholders as the owners of the company, the fact that the company has a separate and independent legal personality from the founders

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11 FREEMAN, R. Edward, Stakeholder Management: A Stakeholder Approach, Pitman/Ballinger, Boston, 1984.

12 POROY, R. / TEKİNALP, Ü. / ÇAMOĞLU, E., Ortaklıklar Hukuku I, 14. Ed., İstanbul, 2019, p. 309-311.

13 The principle of ultra vires that limits the legal capacity of companies to their stated objectives has been abolished by the Turkish Commercial Code enacted in 2012. See TTC Justification of art. 125, p. 42.

14 The fact that the continuation of legal personality does not depend on the personality of its partners also creates constituency for the company. See POROY / TEKİNALP / ÇAMOĞLU (2019) p. 309.

15 PULAŞLI, Hasan, Şirketler Hukuku Genel Esaslar, 5. Ed., Adalet, Ankara, 2017, p. 307.

suggests that the company cannot be owned.[16] For this reason, no company law system focusses solely on maximizing shareholders' return while defining the purpose of the company.[17]

As to Turkish law, there is no specific definition on company's interest, but the law emphasizes that company's interests must be protected, and this can be done through the hands of the board of directors. The board of directors is the single responsible organ with the management and the representation of the company (TCC, art. 365) can carry out all kinds of business and legal transactions on behalf of the company that fall within the company's purpose and the business subject-matter (TCC, art. 371). Under art. 369/1 of the TCC, the provision of "*the duty to act in the company's best interest in good faith*" draws a boundary to the decisions of directors so that personal interests of directors (or others') do not override the interests of the company.[18] In this vein, the duty to act in the company's best interest (i.e., the duty of loyalty) provides a protection of company's interests against of others, such as; directors, controlling shareholders or relatives of controlling shareholders, and other third parties.

It should be noted that the concept of "company interest" is a much broader concept than economic gain.[19] Transactions may be accepted as beneficial for the company even in cases when there is a likelihood positive impact considered or a potential benefit expected to arise in the future.[20] In an ideal world, the interests of the controlling shareholder(s) and the interests of the company are aligned. Yet, there are cases when the conflict between the interests of the company and the shareholders may arise. First, there might be cases when providing particular information to shareholders may potentially harm the company. In such cases, the law

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16 *Ibid*, p. 568-570.

17 Sjafjell describes the concept of shareholders as the owners of the company as a "legal myth". SJAFJELL, Beate, "Beyond Climate Risk: Integrating Sustainability into the Duties of the Corporate Board", Deakin Law Review, 23, 2018, 1-22, p. 49-50.

18 TCC Justification of art. 369/1, p. 111.

19 KIRCA, İsmail / ŞEHİRALİ ÇEVİK, Feyzan Hayal / MANAVGAT, Çağlar, Anonim Şirketler Hukuku C. 1, Ankara, 2013, p. 57.

20 SERDER, Selen, "Anonim Şirketlerde Yönetim Kurulunun İşletme Dışında Kalan İşlemler Nedeniyle Sorumluluğu", Terazi Hukuk Dergisi, 14, 2019, 93-111, p.100.

made it possible for directors to refuse to provide information to shareholders on the grounds of protecting the company's interests. According to the TCC, directors may refuse to provide such information to shareholders if providing the requested information would reveal company secrets or endanger other company interests that need to be protected (art. 437/3). Here, the damage to the company's interest should not be measured only in terms of the loss of tangible assets. The definition of the loss of company interest may include any kinds of risks that may endanger the interests of the company, such as the loss of business opportunities, loss of affiliated companies, loss of customer environment, loss of distribution channels and business relations. Second, there is a risk of seizure of company's assets by the controlling shareholder (i.e., through tunneling) who has a direct control over the finance and a large influence on the board, consequently on company's decision-making on how to use of company's assets. This type of problem is the prevailing corporate governance issue in Turkish companies.[21] Due to the controlling shareholder's influence over the board, the law aimed to place directors under a commitment of loyalty towards the company.[22] In cases where the conflict of interest arises between the company and the controlling shareholder, under the duty of loyalty, directors must take the necessary precautions so that the interests of the controlling shareholders (or their relatives') are not favored instead of the company's.

## II. DIRECTORS' ROLE FOR SOCIALLY RESPONSIBLE COMPANIES UNDER THE BUSINESS JUDGEMENT RULE

Companies, in particular companies with limited liability, accounted for their economic benefit rather than their social values brought by into societies.[23] As the previous section illuminated, the law defined the statutory duties of directors towards the company and kept silent for

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21 YURTOĞLU, Burçin, B., "Ownership, Control and Performance of Turkish Listed Firms", Empirica, 27, 2000, 193-222.

22 The duty of loyalty also detains directors from self-dealing and insider-trading practices. See TCC Justification of art. 369/1, p. 111.

23 SJAFJELL, Beate, "How Company Law has failed Human Rights – And What to Do About It", University of Oslo Faculty of Law Legal Studies Research Paper Series No. 2020-07.

broader social responsibilities. In this section, directors' role for socially responsible companies will be questioned under the business judgement rule.

Much of the academic discussion on the responsible business addressed by the virtue of business ethics[24] and many of the discussion disregarded the role of company law on the matter. As social and environmental concerns have become more salient nowadays, legal compliance[25] as a moral duty is deemed insufficient. Not only with the effects of the global crisis becoming more visible but also with the emergence of the Covid-19 virus epidemic at the global scale, a greater attention has been placed recently on stakeholder interests and the social responsibility of corporations. Nevertheless, it is an uneasy task for directors to embrace social and environmental responsibilities while making sure that they are fulfilling the statutory duties. Moreover, neither the Turkish Commercial Code nor corporate governance guidelines specify the roles and duties of directors for socially responsible business. Concerning broader stakeholder interests, the company law does not clarify any duty on the board. Similarly, the Turkish Corporate Governance Principles narrowly views the social responsibility of a company. Under the section of "relations with stakeholders", it submits that the company should be responsive to its social responsibilities and comply with laws and regulations, and ethical standards (CG Principles, art. 3.5.2). Companies are formed of various corporate constituencies and all stakeholders, including shareholders, employees, customers, suppliers, creditors, communities, and the public at large are critical to the success of businesses. According to the stakeholder governance, beyond shareholders, other stakeholders also contribute to the company and hence their interests should be considered.[26] From

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24 GIBSON, Kevin, "The Moral Basis of Stakeholder Theory", Journal of Business Ethics, 26, 2000, 245-257.

25 PULAŞLI, Hasan, "Compliance Kavramı ve Yönetim Organının Compliance Sorumluluğu", Banka ve Ticaret Hukuku Dergisi, 35(2), 2019, 27-59. See also, YAŞAR, Tuğçe N., "Şirketler Hukuku Açısından 'Compliance' Kavramı ve Borsaya Kayıtlı Şirketlerde Uygulanması", Doktora Tezi, Ankara 2018.

26 FREEMAN (1984). See also MAYER, Colin, Prosperity: Better Business Makes the Greater Good, Oxford University Press, Oxford, 2018.

this point of view, companies should take into account the interests of non-shareholder stakeholders and consider ESG factors when determining their business strategy. Without any doubt neither every company competes in the same regulatory environment, operates in the same industry nor is subject to the harmonious interests and expectations of various stakeholder groups. Thus, the issue of how a company deals with ESG issues in its operations to drive long-term value creation and how to balance the competing interests of various stakeholders requires a company-specific approach which should be vested to directors' discretionary authority.

**A. Business Judgement Rule**

Directors can constantly access valuable inside information and make managerial decisions that will affect the future outlook and the sustainable development of a company. The duties of care and loyalty requires that company directors and managers to act in the company's best interests and perform their duties and responsibilities as defined by law and the articles of association.[27] While performing their duties and responsibilities, company boards enjoy a discretionary authority. The issues of considering ESG factors when developing investment strategies or promoting for a corporate culture that gives high priority to ethical standards and human rights may rest with the board of directors' business judgement as long as it fulfills the conditions.

The business judgement rule was originally developed through case law in Anglo-Saxon law and eventually recognized by the continental European legal systems. In its essence, the concept of business judgement accepts directors as irresponsible for the business decisions that require discretion.[28] The business judgement rule is also acknowledged by the

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27 See section I above.

28 GÖKTÜRK Kürşat, "Amerikan, Alman, İsviçre ve Türk Hukukunda İş Adamı Kararı İlkesi", İnönü Üniversitesi Hukuk Fakültesi Dergisi, 2 (2), 2011, 207- 246, p. 237.

Turkish company law under article 369 of the TCC. Accordingly, directors' business judgement will not be questioned by courts[29] as long as directors act in good faith and not in self-interested way and they should reach out their decisions after careful considerations and investigations made by receiving necessary information.[30] The business judgement rule also enables directors to take business decisions independently and absent from any influence of particular shareholders, such as shareholders with controlling power.[31] Thus, under the business judgment rule, directors will be freed from the liability cases brought by disappointed shareholders.

Directors and managers are not entirely irresponsible when making managerial decisions on matters requiring discretion. The conditions for applying the business judgement rule in Turkish company law are detailed in the doctrine.[32] For a successful business judgement rule defense, directors must act in disinterested and independent manner when taking business decisions. For example, if there is a conflict of interest between the company and board members or their relatives, in such cases, business decisions should be taken according to the "arms' length" principle so that the interests of the company are protected.[33] In other words, if there is personal benefit involved in the business decisions of directors then the business judgement rule would not be applicable. With the condition of disinterested directors, it is ensured that directors who are in conflict with company's interests are not actively involving in the formation of the decision. Other condition for the business judgement rule to be relevant is

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29 KIRCA, İsmail, "Anonim Şirket Yönetim Kurulu Kararlarında Takdir Yetkisi-Özen Borcu", Batider, 22 (3), 2004, 85, p. 87-88.

30 TCC Justification of art. 369, p. 111-112.

31 In case of group of companies, where the parent company directly or indirectly owns all of the voting rights and shares of the subsidiary, directors of the subsidiary are required to follow the decisions of the parent company (TCC, art. 203). The directors of the affiliated company cannot be held liable to the company and its shareholders due to their compliance with these instructions (TCC, art 205). The directors of the subsidiary can only refuse to implement the decision if this will lead to insolvency or liquidity.

32 PULAŞLI (2017) p. 482-486; GÖKTÜRK (2011) p. 238.

33 PULAŞLI (2017) p. 485.

that directors must obtain sufficient information before making business decisions, and if necessary, consult with experts or committees on the subject matter.[34] Lastly, directors must seek the best interest of the company and act in good faith while making business decisions. This condition must be understood as directors' effort in good faith in realizing the company's interests. Under these conditions, the business judgement rule does not oblige directors to achieve a particular economic or business result, as long as they act in good faith to realize the company's interests.

Depending on different perspectives on the corporate entity status,[35] the business judgement rule may be interpreted either narrowly or broadly by the courts. For example, the advocates of shareholder value principle would argue that directors should not decide the corporation to act to benefit employees or the environment unless the decision is in line with shareholder maximization goal. On the contrary, others who see the corporation from a stakeholder approach tend to rewrite the business judgement rule to held corporations accountable to act in a more socially responsible way. From this point, as directly linked to this paper's theme, one may ask to what extent the business judgement rule is applicable to business decisions on ESG-related matters.

### B. Limits Of Directors' Duties For Socially Responsible Business Conduct

Discretionary power of directors on ESG factors is necessary because not every companies' impact on environmental or social issues are identical. Many ESG issues are industry- or company-specific. For example, environmental issues are very much relevant for companies operating in the energy sector than for companies in the service sector. For this reason, a company-based strategic approach is necessary on ESG matters. Depending on the industry and regulatory environment, each corporation needs to adopt a different approach for defining and fulfilling ESG objectives. Determining company specific ESG objectives will serve as a guidance for situations where managers can act at their discretion.

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34 *ibid*.

35 See section I above.

Making social contributions is one of the areas under the purview of discretionary power of directors and managers. There is no specific rule on the appropriate (or socially responsible) business conduct. What are the fundamental elements to determine a socially responsible practice for a company? The answer to this question can be highly subjective. Especially for some cases, the question of which behavior is involved in socially responsible conduct can raise controversy. For example, a company decided that it would be irresponsible to provide health insurance that includes anti-abortion drugs.[36] It is difficult to reach a full consensus on what is responsible business conduct on such controversial issues. In spite of that it is usually the case that business conduct aiming to increase public welfare and education as well as practices engaged for philanthropic purposes deemed as appropriate business conduct. For that matters, the questions of who decides for the company to get involved in such activities and whether managers free to devote a reasonable amount of company resources to such purposes can be asked.

First and foremost, it should be noted that for philanthropic activities involving aids and donations, board of directors cannot enjoy a complete discretion. Especially for donations directed to company employees and workers, there are specific provisions for joint-stock companies to abide under Turkish company law. Accordingly, directors of joint-stock companies can set aside a certain portion of the net profit as a donation fund in the articles of association for the establishment or maintenance of aid organizations for the company's employees and workers (TCC, art. 522/1).[37] It is also possible this reserve fund to be given for public legal entities or otherwise the company should establish a foundation or a cooperative for the same purpose (TCC, art. 522/2). Even if there is no provision stipulated in the articles of association, the law permits the general

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36 *Burwell v. Hobby Lobby Stores, Inc*., 573 U.S. 682, 711-712 (2014). See also HAZEN, Thomas Lee, "Corporate and Securities Law Impact on Social Responsibility and Corporate Purpose" available at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3542833 Accessed 20.01.2021 p. 2.

37 Article 521 of the TCC regulates the certain portion of the company revenues to be kept aside as obligatory reserve fund. This article also admits companies to make such reservations by the articles of association.

assembly to set aside reserves from the net profit in order to establish or maintain aid funds and other aid organizations for the company's employees or to serve for other kind of aids and purposes for charity (TCC, art. 523/3). From these regulations, it is understood that the law permits directors to consider aids and donations only for the company's employees and workers through establishing a foundation or making these donations to a public legal entity. Other than that, the decision of the general assembly is required for making donations and involving other philanthropic activities including the establishment of a foundation for these purposes.[38]

There are contradictory arguments put forward in the literature with regards to directors' capacity for socially responsible activities to be carried out for interest groups that are not bound to the company by a contract. According to some scholars, directors are unauthorized to consider ESG-related issues.[39] They argue that the general assembly's decision is essential for companies to be involved in socially responsible activities. According to this view, only legal transactions made by directors that deemed reasonable to the financial situation of the company, such as donations for cultural purposes, can be accepted as legal.[40] On the contrary, others hold that directors' decisions on the company's social contributions in the form of donations can be considered as valid if the interests of the company are protected, even if there is no provision stipulated in the articles of association.[41] In the same manner, the Court of Cassation (*Yargıtay*) established that donations that are not within the scope of the

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38 ADIGÜZEL, Burak, "Anonim Şirketlerde Bağış ve Yöneticilerin Sorumluluğu", Terazi Hukuk Dergisi, 14, 2019, 58-67, p. 60.

39 KARAYALÇIN, Yaşar, Ticaret Hukuku Dersleri, Şirketler Hukuku, Ankara, 1965, p.132 in ADIGÜZEL (2019) p. 61; ÇEVİK, Nuri Osman, "Ticaret Şirketlerinin Bağışta Bulunabilme Ehliyeti", Ankara Barosu Dergisi, 1991, p. 560 in ADIGÜZEL (2019) p. 61.

40 İMREGÜN, Oğuz, Anonim Ortaklıklar, İstanbul, 1989, p. 40 in ADIGÜZEL (2019) p. 61; YILDIZ, Burçak, "Şirketlerin Ehliyetine İlişkin Olarak Özellik Arz Eden Bazı Hukuki İşlem ve Sözleşmeler", Ankara Barosu Dergisi, C.2, 2006, p. 75-76 in ADIGÜZEL (2019) p. 61.

41 POROY, Reha / TEKİNALP, Ünal / ÇAMOĞLU, Ersin, Ortaklıklar ve Kooperatif Hukuku, 11. Ed., İstanbul, 2009, p. 101 in ADIGÜZEL (2019) p. 61.

business subject matter and not protecting the interests of the company are deemed as void.[42]

In the light of these, it can be concluded that the discretional authority of directors on ESG-related issues is bound with the limits of the business subject matter of the company.[43] As a matter of fact, the law determined the business subject matter of the company as the legal limit of the representation authority for directors (TCC, art. 371/1).[44] Accordingly, the board of directors may be able to consider economic contributions in the areas related to social or environmental issues on the grounds that these transactions are within the scope of the business subject matter of the company.[45] Within these limits, directors are able to make donations without the approval of the general assembly.[46] If the internal directive does not require a decision of the board of directors, the decision for a donation can be reached with double signature (TCC, art. 370/1).[47]

It is believed that donations to be used for scientific purposes can be considered as legal because the society expect these considerations

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42 Court of Cassation (*Yargıtay*) overruled a company's donation to a political party by recognizing this as not in the subject matter of the company. See Y. HGK. T. 29.11.1969 1966/T-1396 E. 1969/847 K. in ADIGÜZEL (2019) p. 61.

43 The scope of the business subject matter of the company is stipulated in the articles of association. However, this concept should be interpreted broadly and apart from the areas stipulated in the articles of association, other fields of operation that produced by doing business should also be considered within the scope of the business subject matter. See POROY/TEKİNALP/ÇAMOĞLU (2019) p. 241.

44 Those authorized to represent the company are directors, general managers and third parties who have been given the authority to represent the company (TCC, art. 370/2). Since the ultra vires rule has been abandoned, transactions other than the company's purpose and the business subject matter also bind the company, however, the company may request recourse against directors who exceed the legal limit of their representative authorities. See TCC Justification of art. 371, p. 113.

45 ADIGÜZEL (2019) p. 62-63.

46 Before deciding the nature and the size of the donation, the board of directors should consider the size and the financial situation of the company. In this respect, in line with the art. 408/2/f of the TCC, it is not possible for the board of directors to donate a significant amount of the company's assets without the approval of the general assembly. See *ibid,* p. 63.

47 A decision of the board of directors might be required as necessary for considerations that are materially important for the company and employed doubts with regards to company's interests. See *ibid,* p. 62.

from companies as a requirement for a moral obligation.[48] Under this moral obligation, directors are able to consider donations for improving the general welfare of the society, including the protection of the environment or the elimination of diseases such as the whole world experienced in the case of the global pandemic resulted by the Covid-19 virus.[49] It is important to note that these kind of donations should be made within reasonable limits according to the size, net profits and financial situation of the company.[50] Otherwise, these social contributions may be considered as against the interests of the company and therefore, the liability of directors may arise.[51]

For directors of publicly held joint-stock companies, the discretion of considering social contributions is more restrictive. According to the Turkish Capital Markets Law, the conditions for making donations must be stipulated in the articles of association (art. 19/5). In this respect, the upper limit of donations is determined either by the articles of association or by a decision of the general assembly; and the board of directors are not allowed to decide to make a donation in excess of this upper limit.[52] A decision making such aid or donation requires the approval of the general assembly. Also, the board of directors should inform shareholders at

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48 TEKİNALP, Ünal, Anonim Şirketlerin Bilançosu ve Yedek Akçeleri, 2. Bası, İstanbul, 1979, p. 368 in ADIGÜZEL (2019) p. 63.

49 For the case examples of companies involving socially responsible activities during the Covid-19 crisis see KANDEMİR, Hatice Kübra, "Covid-19 Measures Adopted by the Provisional Article 13 of the Turkish Commercial Code on the Limitation of Companies' Dividend Distribution Decisions: The Corporate Objective Debate Revisited" in Covid-19 & The Society: Socio-Economic Perspectives on the Impact, Implications, and Challenges, Polat, M., / Burmaoğlu, S. / Sarıtaş, O. (eds), Springer *forthcoming* 2021.

50 ADIGÜZEL (2019) p. 64.

51 The business judgment principle will not be applicable for the cases where a decision is taken against the law and the articles of association, thus a liability lawsuit may be filed against the board of directors. See PULAŞLI, Hasan, "Kurumsal Sosyal Sorumluluk Bağlamında Uluslararası İnsan Hakları ve Çevre Standartlarının Çok Uluslu Şirketlerin Merkez Yönetim Organının Hukuki Sorumluluğuna Etkisi", Banka ve Ticaret Hukuku Dergisi, 36(4), 2020, 5-37, p. 28.

52 Communique on Dividends Series (II-19.1), 23.01.2014, Official Gazette No: 28891, art. 6.

the general assembly about the amount and beneficiaries of all donations and aids made (CG Principles, art. 1.3.10).

Further it can be asked whether directors free to consider ESG-related conduct even though such practices would result in loss in profits? If directors adopt a strategy based on ESG issues on the detriment of shareholders,[53] it is expected that this will be most likely result in replacing directors by the shareholders' votes at the general assembly and shareholders asking for damages. The following example demonstrated a different course. In 2014, directors at CVS Health (CVS Caremark)[54] decided that the company to stop selling tobacco products in its pharmacies. Following this decision, it was estimated that the company would lose about $2 billion in revenues.[55] As a health care company, directors at CVS made a business decision considering the future growth of the company through ceasing selling tobaccos and declared this decision as "*the right thing to do*".[56] Even though at the time this decision resulted lost in revenues thereby reduction in shareholders' dividends, it was welcomed by many for helping the creation of a healthier future for the society.[57]

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53 It is argued that corporate social responsibility often conflicts with the interests of shareholders, since the transfer of assets to social responsibility activities will eventually result in a loss of the shareholders' share of profit. See PULAŞLI (2020) p. 25.

54 CVS Caremark changed its corporate name as CVS Health. The company is one of the largest pharmacy retailers in America with around 7.600 stores by October 2014. See CSR Health website https://www.cvshealth.com/about/facts-and-company-information Accessed 20.02.2021.

55 George ANDERSON, "Can CVS Justify Its No-Tobacco Decision Beyond the Great PR?" February 5, 2014 Forbes https://www.forbes.com/sites/retailwire/2014/02/05/can-cvs-justify-its-no-tobacco-decision-beyond-the-great-pr/?sh=5dd81bd13fe0 Accessed 20.01.2021.

56 In an official statement, the CEO, Larry Merlo stated that the sale of tobaccos is inconsistent with the purpose of the company. https://www.cvshealth.com/thought-leadership/message-from-larry-merlo-president-and-ceo# Accessed 20.01.2021.

57 The company is still run by the same CEO. As of today, the company has more than 9.900 retail stores in 49 states in the United States, in Columbia and in Porto Rico. See CSR Health website https://www.cvshealth.com/about/facts-and-company-information Accessed 20.01.2021.

The above case illustrates a broader interpretation of the business judgement rule for the sake of directors' discretion. As the business judgment rule establishes, it is at director's discretion how to serve company's interests. The board of directors' role is to determine a business strategy[58] in order to realize the purpose of the company. This business strategy could be in the form of maximizing shareholders' wealth and as long as they act in good faith, directors should be able to determine what it means to maximize shareholder wealth and their method should not be questioned.[59] On the contrary, under a different business strategy, the board of directors could decide to pursue long-term stability for societal benefits and harvesting profits in the long run. Either ways, under the business judgement rule, the legitimacy of directors' judgement should not be questioned by courts or controlling shareholders. Directors should be able to have discretion whether to seek short-term profits for shareholders who expect regular dividends, or long-term stability for societal benefits.[60] Therefore, the means of such practice can be left to directors' discretionary powers under the business judgment rule.

Another area left to the discretion of directors is reporting on non-financial information. Public disclosure plays an important role in acquiring non-financial information, including environmental, social, and human rights-related issues. In Turkey, according to the regulations of the Capital Markets Board (CMB), listed companies must publish a compliance report, as separately attached in the annual report of the company, disclosing their compliance and the reasons for non-compliance with the

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58 The management of the company is among the indispensable and unassignable authorities of the board of directors (TCC, art. 345). This managerial duty includes adopting the company's managerial strategies. See POROY / TEKİNALP / ÇAMOĞLU (2019) p. 364.

59 FERSHEE, Joshua Paul, "This, I Believe: A New Look at Corporate Purpose, Director Primacy and the Business Judgment Rule", Transactions: The Tennessee Journal of Business Law, 21, 2020, 301-310, available at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3689236 Accessed 27.01.2021.

60 *ibid*, p. 303.

Corporate Governance Principles.[61] In terms of disclosure on environmental and social issues, public companies are required to disclose their corporate-social-responsibility (CSR) policies and report accordingly their activities in the corporate governance compliance report. Accordingly, companies must disclose the information in annual reports about the social rights of employees, professional training and other corporate social responsibility issues related to the activities of the company that have social and environmental impact.[62] However, the CSR reporting is not compulsory for companies instead it is based on comply or explain principle; meaning that companies are accepted to comply with the rule and explain the reasons for any departure. Article 3.5.2 of the CG Principles states a similar approach on board's responsibility on this matter by stipulating the responsibility to act in accordance with the law and ethics. The provisions related to sustainability and social responsibility of companies are not mandatory to comply for public companies. Public companies only have to make a statement in their annual reports about non-compliance and explain the general policy on these matters. It is usually the case that companies provide statements that rather vague and almost identical with other firms' explanations.

More recently, On October 2, 2020, the CMB issued an amendment to the Corporate Governance Communique and introduced a new requirement for public companies under the "Sustainability Principles Compliance Framework" to provide information on Environmental, Social and Governance (ESG) activities.[63] Under this new framework, in their annual reports public companies are required to explain on a voluntary basis whether they applied the sustainability principles and if not, to

61 Corporate Governance Communiqué Series (II-17.1), 03.01.2014, Official Gazette No: 28871, art. 8 (1).

62 CG Principles, art. 2.2.2(g).

63 Communication (II-17.1. a) regarding the amendments to the Corporate Governance Communique (II-17.1), 02.10.2020, Official Gazette No:31262.

provide an explanation on risk management of the impacts of environmental and social impacts of not complying the principles.[64] At the EU level, the requirements of non-financial reporting are regulated by the Directive 2014/95/EU (amending Directive 2013/34/EU) making non-financial reporting compulsory for certain large undertakings, i.e., companies that have employees more than 500 to disclose ESG reporting.[65] In terms of the reporting standards to comply, the Directive leave discretion to companies to choose from different versions of ESG reporting. The Directive only refers to "material" information to be included in the reporting and it allows companies to determine what is "material". Similarly, the CMB of Turkey recognizes different international standards on non-financial reporting issued by different organizations, such as Global Reporting Initiative (GRI), International Integrated Reporting Council (IIRC), and Sustainability Accounting Standards Board (SASB), and makes room for companies to choose their method of reporting. This flexibility attributes directors and managers a vital role in determining and disclosing the material information in sustainable reporting.

In practice, reporting on social and environmental issues to a large extent based on voluntary action and companies usually viewed it as a way of marketing activity.[66] So far, reporting on social responsibility activities of companies largely remain limited to the purpose of marketing or at best increasing reputation as a form of public relations.

**CONCLUSION**

This paper illustrated the limits of the role and responsibilities of directors of joint stock companies on corporate social responsibility within the scope of Turkish company law. In this context, it is seen that

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64 Sustainability Principles Compliance Framework, A. General Principles, A.1 Strategies, Policies and Goals https://www.spk.gov.tr/Sayfa/Dosya/1332 Accessed 17.01.2021.

65 Directive 2014/95/EU of the European Parliament and of the Council of 22 October 2014 Amending Directive 2013/34/EU as Regards Disclosure of Non-Financial and Diversity Information by Certain Large Undertakings and Groups, OJ L330/1. 15.11.2014.

66 CETINDAMAR, Dilek, "Corporate Social Responsibility Practices and Environmentally Responsible Behavior: The Case of The United Nations Global Compact", Journal of Business Ethics, 76, 2007, 163-176.

while company law regulations determine the statutory duties of directors towards the company and its shareholders, there are no rules stipulated on social and environmental responsibilities.

In case of engaging socially responsible activities, within the scope of article 523/3 of the TCC, members of board of directors and managers of joint-stock companies are able to consider donations with regards to those who are bound by a contract to the company, i.e., the company's employees and workers. However, the law does not grant authority to directors to consider charitable activities or by reserving reserves for this purpose, unless it is decided at the general assembly. Similarly, for public joint stock companies, only donations that subject to an upper limit determined by the general assembly can be made on the condition that there is a provision in the articles of association.

Apart from these regulations, as this paper submitted, it is possible for directors using their discretionary authority on ESG-related issues under the business judgement rule. For the validity of these decisions certain conditions can be determined. When making decisions regarding socially responsible business conduct, first of all members of the board of directors and managers are bound to act as a cautious manager, to pursue the best interest of the company and act in good faith under art. 369 of the TCC. Subject to these statutory duties, directors and managers of a company can take decisions on social and environmental issues in accordance with the business judgment rule, provided that these deeds are within the scope of the company's subject matter and the long-term interests of the company are prioritized. The validity of these decisions will depend on directors acting independently of their personal interests.

If a certain amount of company resources decided to be devoted for socially responsible business conduct, for example investing in production methods to reduce the company’s negative environmental impact in the field of production, it would be appropriate to determine this amount by taking into account the size and financial status of the company at the time. Although the term of the business subject matter is said to be interpreted broadly, directors’ responsibilities may arise for decisions falling out of the scope of the business subject matter; if demonstrated that the

conditions of the business judgment rule has not been met and directors have failed to fulfill the duty of care.

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