

**# CORPORATE GOVERNANCE FOR SUSTAINABILITY: THE
NECESSARY REFORM OF TURKISH COMMERCIAL LAW**
(SÜRDÜRÜLEBİLİRLİK İÇİN KURUMSAL YÖNETİM: TÜRK TİCARET
KANUNU'NDA REFORMUN GEREKLİLİĞİ)

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ÖZ

Türkiye'de kurumsal yönetim söylemi, çoğunlukla asil-vekil konularına odaklanan Anglo-Sakson hukuku ve ekonomi düşünce tarzından esinlenmiştir. Bu nedenle, düzenlemeler hissedarlar getirilerinin kısa vadeli maksimizasyonuna odaklanmıştır. Ancak, Türk şirketler hukukunun mevcut odak noktası, sürdürülebilir şirket gelişimini engelleyen bir boşluk barındırmaktadır. Kâr maksimizasyonu odağının bir sonucu, şirketlerin çevresel ve sosyal konuları dikkate almaması ve bunları stratejik planlarına entegre etmemesidir.

Türkiye, 2012 yılında Türk Ticaret Kanunu'nda yapılan reformdan bu yana kurumsal yönetimin düzenleyici çerçevesinde büyük bir ilerleme kaydetmiştir. Ancak, kurumsal sürdürülebilirlik hala ele alınması gereken bir konudur. Bu kapsamda, Türkiye Sermaye Piyasası Kurulu tarafından Sürdürülebilirlik İlkelerine Uyum Çerçevesi hazırlanarak 02.10. 2020 tarihinde yürürlüğe konulmuştur.

Bu çalışma, sürdürülebilirliğin Türkiye'nin kurumsal yönetim ilkelerine entegrasyonunun yasal dayanağını araştırmayı ve kurumsal sürdürülebilirliğin önündeki engelleri ortaya çıkarmayı amaçlamakta ve bunların sonucunda tamamlayıcı reform önerileri sunmaktadır. Sürdürülebilirlik İlkelerine Uyum Çerçevesi, yasama girişimlerinde bir başlangıç noktası olması bakımından yararlıdır. Bu makalenin öne sürdüğü argüman ise daha iyi bir uyum sağlanması için aşağıdaki noktaların ele alınması gerektiğidir; şirketin amacının şirketler hukuku kapsamında yeniden düzenlenmesi, kurumsal sürdürülebilirliğin yönetim kurulunun

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görevlerine entegre edilmesi ve raporlama ve denetim standartlarının belirlenmesi.

Anahtar Kelimeler: Kurumsal Yönetim, Sürdürülebilirlik, Kurumsal Sürdürülebilirlik, Yumuşak Hukuk

ABSTRACT

The corporate governance discourse in Turkey is inspired by the Anglo-Saxon law and economics way of thinking, which mostly focuses on principal-agency issues. Thus, much attention has been paid to the short-term maximization of returns to shareholders. However, the current focus of the Turkish commercial law gives rise to a loophole that prevents the development of sustainable business. The result of profit maximization focus is that corporations fail to consider environmental and social issues and integrate them into their strategic planning.

Turkey has made a great progress in regulatory framework of corporate governance since the reformation of the Turkish Commercial Code in 2012. Yet, corporate sustainability still remains to be addressed. In this context, the Sustainability Principles Compliance Framework is prepared and put into effect by the Capital Markets Board of Turkey on 02.10. 2020.

This study aims to investigate the legal basis for the integration of sustainability into corporate governance principles of Turkey and to reveal the barriers to corporate sustainability and as a result it offers complementary reform proposals. The Sustainability Principles Compliance Framework is useful, insofar as it feature as a starting point in legislative initiatives. The argument this article puts forward is that in order for a better compliance, the following points need to be adressed; reformulating the purpose of the company in the company law, integrating corporate sustainability into the duties of the board of directors and determining clear reporting and auditing standards.

Keywords: Corporate Governance, Sustainability, Corporate Sustainability, Soft Law

Introduction

Corporate governance is a discipline on its own. Given the developing nature of the corporate governance, defining this concept is not an easy task. The debate on the definition is intellectually interesting.¹ Depending on the point of view, the content may be treated in a narrow or broad manner. The traditional view expresses that corporate governance is the relationship between a company and its shareholders. This narrow view is expressed in *agency theory* propounded by the Cadbury Report, in which corporate governance is defined as a *system by which companies are directed and controlled*.² The ones who adhere to this view see the corporation as the property of the shareholders and advocate that the only legitimate purpose of the corporation is to make money for its shareholders.³ This legitimate purpose of corporation is expressed by Berle as ‘*all powers granted to a corporation or to the management of a corporation, or to any group within the corporation... [are] at all times exercisable only for the rateable benefit of all the shareholders as their interest appear*.’⁴ This perceived obligation of profit maximization for shareholders is in the heart of conventional corporate governance view.

At the other side of the debate, corporate governance is seen as a web of relations between the company and its stakeholders. It is argued that corporation is not only creating value for shareholders but also for stakeholders, such as employees, customers, suppliers and so on. The debate over the corporations’ duty is whether to maximize shareholder value or seek to serve for the whole society remains unresolved.⁵ Going deeper into this debate would probably not reach to any change in the normative basis of the purpose of the company as long as the company law in a certain

¹ Elhabib, M.A., Rasid, S.A. and Basiruddin, R. (2014) “A critique: Corporate governance definition dilemma and the major causes for calls to improve corporate governance”, *European Journal of Business and Management*, 6(34), 365-369.

² Report of The Committee on The Financial Aspects of Corporate Governance (1992) <https://ecgi.global/sites/default/files/codes/documents/cadbury.pdf>

³ Smith, D.G. (1998) “The shareholder primacy norm”, *Journal of Corporation Law*, 23, 277-322.

⁴ Berle, A.A. (1931) “Corporate powers as powers in trust”, *Harvard Law Review*, 44(7), 1049-1074.

⁵ Rock, E. (2020) “For Whom is the Corporation Managed in 2020?: The Debate over Corporate Purpose”, *European Corporate Governance Institute - Law Working Paper No. 515/2020*.

https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3589951

jurisdiction does not support the broader understanding of corporate governance.

As stated in the foreword of the Organization for Economic Cooperation and Development (OECD) Corporate Governance Principles, ‘*corporate governance principles are a living instrument offering non-bind standards and good practices as well as guidance on implementation, which can be adapted to the specific circumstances of individual countries and regions.*’ This statement signals that corporate governance should be understood as principles that are continuously evolving along with the needs of the business world. Thus, once a state has reached a certain level of corporate governance, either by voluntarily or compulsory implementation, it must take a step forward.

Even though the introduction of corporate governance as a concept in Turkey does not have a long history, the Turkish government has already worked to address the corporate governance challenges via a wide range of commercial law reforms in the last decade. Meanwhile, the global business trends focused on the necessity of establishing a culture of sustainability in the businesses, which deals with social and environmental issues as well as economic ones. The last decade has also witnessed a growing number of investors seeking to make investments in line with both their financial goals and personal values.⁶ This means that while investors aim to maximize their financial returns, they avoid investing in harmful companies. To catch up with the novelties in the business world, it became necessary for Turkey to incorporate the concept of sustainability to its corporate governance framework.

This study starts with revisiting conventional -shareholder oriented- understanding of corporate governance in Turkey and discuss a more important question: How the integrated sustainability principles to corporate governance regulation in Turkey are better complemented? To answer this question, corporate governance in Turkey is summarized. Thus, it is seen that compliance of Turkish companies with the principles of corporate governance reached to a certain level, which shows that it is time to go a step further. This step is to integrate sustainability into the corporate governance understanding of Turkey. The following parts investigate the concept of sustainability in corporations and motivations in international

⁶ McKinsey. (2017) “From ‘why’ to ‘why not’: Sustainable investing as the new normal” <https://www.mckinsey.com/industries/private-equity-and-principal-investors/our-insights/from-why-to-why-not-sustainable-investing-as-the-new-normal#>.
YÜHFD Cilt: XIX Sayı:2 (2022)

area. After giving the nexus between corporate sustainability and the Turkish Law, shortcomings of the Sustainability Amendment of Corporate Governance Communiqué are determined. Before the conclusion, some complementary amendments are proposed.

Sustainability in Corporations

The traditional finance view suggests that maximizing shareholder profit is the main purpose of the corporations.⁷ It is advocated that managers should only pursue profit maximization and exclude other objectives as long as they contravene with this purpose. In contrast to this view, some scholars stated that a company is a private entity which has liabilities to the public.⁸ Even though they accepted that without profits companies would go bankrupt, profit should not be assumed to be at the expense of everything else for the simple reason of profit maximization. Indeed, the company must fulfill a level of societal objectives. The early research suggests that companies should be accountable to all its participants, rather than only shareholders, by including non-financial information in their financial tables.⁹ This view have been extensively criticised stating that stakeholder oriented accountability sacrifice shareholder value.¹⁰ Today, the perception of taking sustainability in the corporate agenda runs counter to the expectations of the shareholders is outdated. Today, companies use the ‘Triple-Bottom-Line’ concept in their activities in order to strike a balance between financial success and social goals and sustainable environmental compatibility. In this case, the aim of public joint stock companies should be, at the same time in a balanced way, to maximize profit, to have an awareness of social responsibility that takes into account the interests of the company and its employees, and to realize an economy that ensures

⁷ Jensen, M.C. (2002) “Value maximization, stakeholder theory and the corporate objective function” *Business Ethics Quarterly*, 12(2) 14, 8-21

⁸ Sjøfjell, B. (2017) “Regulating for corporate sustainability: Why the public-private divide misses the point” in B. Choudhury & M. Petrin (Eds.), *Understanding the company corporate governance and theory* (pp 145-164). Cambridge, UK: Cambridge University Press.

⁹ Gray, R., Owen, D. & Maunders, K. (1987) *Corporate social reporting: Accounting and Accountability*, London Prentice-Hall International.

¹⁰ See Sternberg, E. (2002) “The defects of stakeholder theory” *Corporate Governance: An International Review*, 6 (3), 151-63 and Freedman, R.E. & Reed, D.L. (1983) “Stockholders and stakeholders: A new perspective on corporate governance”, *California Management Review*, 25(3), 88-106

efficiency and respect for human rights.¹¹ Thus, the ‘Triple-Bottom-Line’ concept corporate sustainability are closely linked. Research shows that sustainability is among the investment criteria of many investors in developed states.¹² Hence, the concept of sustainability should take place in the corporations’ strategic planning and reports in order to attract investors.

The term sustainability is a controversial issue and thus, has many definitions. A widely accepted definition is given in the Brundtland Report as "*Sustainable development is development that meets the needs of the present without compromising the ability of future generations to meet their own needs.*"¹³ Based on this definition, it is stated that *companies should consider the future (as well as the present) in their decision-making and actions, with the aim of using their resources for creating value in the long run to be sustainable corporations.*¹⁴ It is also added that corporate sustainability creates a mutually dependent relation between economic, social and environmental responsibilities of the corporation in order to create value for all its stakeholders in long-term.¹⁵ In this context, creating economic value by production only is not enough for a company to become sustainable. To do so, they should work to minimize the negative effects they cause to environment and society while operating their activities. Therefore, corporate sustainability, which is based on correct use and maintenance of resources of current generations for the needs of future generations, is directly related to economic, social and environmental issues.¹⁶ If all these limited resources are not used correctly today, they will

¹¹ Pulaşlı, H. (2020), “Kurumsal Sosyal Sorumluluk Bağlamında Uluslararası İnsan Hakları ve Çevre Standartlarının Çok Uluslu Şirketlerin Merkez Yönetim Organının Hukuki Sorumluluğuna Etkisi” *Banka ve Ticaret Hukuku Dergisi*, C. XXXVI, S. 4 s. 5-37

¹² Eccles, R.G. & Klimenko, S. (2019) “The investor revolution”, *Harvard Business Review*, 106–116.

¹³ United Nations, Report of the World Commission on Environment and Development: Our Common Future (1987) <https://sustainabledevelopment.un.org/content/documents/5987our-common-future.pdf> (accessed on 22.03.2022)

¹⁴ Salvioni, D.M., Gennari, F. & Bosetti, L. (2016) “Sustainability and convergence: The future of corporate governance systems?”, *Sustainability*, 8(11), 1203-1228

¹⁵ Ibid.

¹⁶ Camilleri, M.A. (2017) “Corporate sustainability and responsibility: creating value for business, society and the environment”, *Asian Journal of Sustainability and Social Responsibility*, 2, 59–74.

YÜHFD Cilt: XIX Sayı:2 (2022)

not be available for future use.¹⁷ At this point, the responsibility of companies towards society regarding sustainability becomes more apparent. Sustainability requires companies to think about what and how they produce while they create long-term shareholder value by covering opportunities and managing risks deriving from economic, environmental and social concerns and to be transparent and accountable in these regards. This is the link between sustainability and corporate governance. Integration of sustainability approach to the operation and culture of companies can be achieved via corporate governance principles. This relation is also supported by Blackburn who states that sustainability is the most appropriate concept that can be said in addition to the consistency of a company's financial success.¹⁸

Motivations for Sustainability in Corporate Setting

The necessity of not only managing the present well but also planning and creating value for the future has taken its place in international arena. With the intention of stimulating the debate on corporate sustainability at the European Union (EU) level, in 2018 report on Sustainable Finance which marked the relationship between corporate governance and sustainability, was published by the High Level Expert Group on Sustainable Finance.¹⁹ The report emphasised that before giving a long-term investment decision, investors and creditors need to understand the risks related to unsustainable business operations and their potential interests in taking sustainability into account. Following this report, on 8 March 2018, the European Commission published an Action Plan for Financing Sustainable Growth in order to mobilise finance for sustainable growth.²⁰ The main objective of the action plan was to include sustainability practices within the guarantee of the corporate governance principles in order to integrate sustainable considerations into financial policy framework. These

¹⁷ Crowther, D. & Rayman-Bacchus, L. (2016). The future of corporate social responsibility. In Crowther, D. & Rayman-Bacchus, L. (Eds.). Perspectives on corporate social responsibility (pp 229-249). Oxon, UK: Routledge.

¹⁸ Blackburn, W. R. (2015) The sustainability handbook: The complete management guide to achieving social, economic, and environmental responsibility. Washington, USA: Eli Press.

¹⁹ The EU High Level Expert Group on Sustainable Finance: Financing A Sustainable European Economy (2018) https://ec.europa.eu/info/sites/default/files/180131-sustainable-finance-final-report_en.pdf (accessed on 21.03.2022)

²⁰ The European Commission Action Plan Financing Sustainable Growth Assessment of The Reform Areas for Pri Signatories <https://www.unpri.org/download?ac=5173> (accessed on 21.03.2022)

intentions to strengthen policy towards integrating sustainability as a key element of corporate governance show that the EU takes concrete steps in order to shift corporate governance priorities to sustainability.

Financial reporting has long been a mandatory and standardized instrument for accountability thanks to the International Financial Reporting Standards (IFRS). However, this is not the case for non-financial reporting. In order to reach a standard in the reporting of non-financial information, the EU adopted The EU Non-Financial Reporting Directive (EU NFRD) in 2014.²¹ It was required to be transposed into the national laws by 2016, with companies obliged to provide enhanced disclosure from 2017 onwards. Thus, a soft law implementation became a legal obligation. As per the EU NFRD, the large companies have to state the policies they implement in their reports in relation to environmental protection, social responsibility and treatment of employees, respect for human rights, anti-corruption and bribery and diversity on company boards. Even though the EU NFRD gives significant flexibility on how to disclose relevant information, Article 2 specifies that non-financial matters must be disclosed to the '*extent necessary for an understanding of the undertaking's development, performance, position, and impact of its activity*'.

Furthermore, the United Nations (UN) took a step and adopted the 2030 Agenda for Sustainable Development with all its members.²² The agenda includes 17 Sustainable Development Goals and 169 targets. The goals of the UN are not only limited to the financial topics but also a wider set of economic, environmental, social and legal topics that have impact on companies. All these initiatives lead the EU states to align sustainability and corporate governance legally.

Recently, the IFRS Foundation accepted sustainability as a global challenge. In Consultation Paper on Sustainability Reporting 2020, it is stated that there is a growing focus on how companies perform and report on sustainability.²³ It is also reported that there is an increasing number of calls for standardization and comparability of reporting on the matter. Although many important initiatives exist at the regional level, when the challenge is global, the most optimal would be implementing global

²¹ Directive 2014/95/EU

²² United Nations, (2015) Transforming our world: the 2030 Agenda for Sustainable Development <https://sdgs.un.org/2030agenda> (accessed on 21.03.2022)

²³ IFRS, Consultation Paper on Sustainability Reporting 2020 <https://www.ifrs.org/content/dam/ifrs/project/sustainability-reporting/consultation-paper-on-sustainability-reporting.pdf>
YÜHFD Cilt: XIX Sayı:2 (2022)

solutions together with the regional initiatives. The IFRS Foundation has decided to look at sustainability as a separate topic and taken a role in the process of standardization since it is working on financial reporting standards which are implemented fully or partly in 144 jurisdictions around the world. As a result of their report, the IFRS Foundation called for a new, separate sustainability board which would take place alongside the international accounting standards board within the IFRS Foundation and made call for public authorities, global regulators and other market stakeholders to support the suggested board in order for it to achieve global consistency and reduce complexity in reporting.²⁴ The report reiterates that this is a demand driven process. Thus, the IFRS standards will move forward as the demand for companies to report on sustainability exists. In sum, the IFRS Foundation encourages states to participate in this consultation.

Contemporaneously, the World Economic Forum stated that the concept of sustainability is gaining currency since businesses and their stakeholders started to recognize that continuity and financial success of businesses depend on their participation in the development of sustainable business operations. In order to participate in this process, businesses and investors should focus on a broader perspective which takes into account all the stakeholders instead of an investor-only perspective. To move discussions further and to embrace policy consistent with an integrated understanding of business sustainability, a core set of common metrics and disclosure on non-financial factors were developed and published.²⁵

Even though the importance of disclosing sustainability performance is understood for the continuity of the businesses, the complexity surrounding sustainability disclosure has made it difficult to develop the comprehensive solution for corporate reporting. In response to this, five standard-setting institutions of international significance, namely Carbon Disclosure Project, Climate Disclosure Standards Board, Global Reporting Initiative, International Integrated Reporting Council and Sustainability Accounting Standards Board, published a joint statement on the elements necessary for

²⁴ IFRS Foundation. (2020) Consultation Paper on Sustainability Reporting, September 2020. <https://cdn.ifrs.org/-/media/project/sustainability-reporting/consultation-paper-on-sustainability-reporting.pdf> (Accessed on 20.03.2022)

²⁵ World Economic Forum. (2020) Measuring Stakeholder Capitalism Towards Common Metrics and Consistent Reporting of Sustainable Value Creation White Paper http://www3.weforum.org/docs/WEF_IBC_Measuring_Stakeholder_Capitalism_Report_2020.pdf (Accessed on 20.03.2022)

more comprehensive corporate reporting.²⁶ This is important because the collaboration of these institutions is an indicator of the urgent need for globally accepted comprehensive corporate reporting standards.

Collaboration between all these standard setting institutions supports the progress towards comprehensive sustainability in corporate setting. The policy and the practice of sustainability in Turkey are also influenced by the growing attention of international institutions on sustainability.

Corporate Governance in Turkey

Cadbury Report advised companies to interpret corporate governance as a balance between economic, social and individual purposes; encouraging effective use of resources and accountability in the management of resources; the equal and balanced consideration of the interests of individuals, companies and society. Developing states met corporate governance principles thanks to the demands of international investors who want to ensure the return of their investments in these states.²⁷ Keeping up with the international developments in the field of corporate governance together with the aim of attracting international investors to its stock market, the Capital Markets Board of Turkey (CMB) issued the corporate governance principles by taking reference the OECD Corporate Governance Principles in 2004.

As the OECD Corporate Governance Principles are non-binding and can be adapted to specific circumstances of individual states, implementation of the principles may vary according to the system of corporate ownership and other factors prevailing in a state. The Turkish corporate structure points to the fact that the Turkish governance model varies from the OECD model of corporate governance. The majority of companies listed on the stock exchange in Turkey remain family-owned. The organization of companies is generally in the form of pyramids of control and the majority shares are concentrated in the hands of a small number of shareholders. In practice, most Turkish companies have controlling minority structure, which is characterised by the existence of one or more shareholders, most are generally family-members, and owning controlling blocks of shares.

²⁶ CDP, CDSB, GRI, IIRC & SASB.(2020) Statement of Intent to Work Together Towards Comprehensive Corporate Reporting <https://29kjwb3arnds2g3gi4lq2sx1-wpengine.netdna-ssl.com/wp-content/uploads/Statement-of-Intent-to-Work-Together-Towards-Comprehensive-Corporate-Reporting.pdf> (Accessed on 20.03.2022)

²⁷ Das, P. (2014) "The Role of Corporate Governance in Foreign Investments", *Applied Financial Economics*, 24(3), 187-201
YÜHFD Cilt: XIX Sayı:2 (2022)

Besides, cross-ownership is widely used in many company groups.²⁸ Thus, a widespread shareholding of companies in a developed capital market does not exist in Turkish capital market. As a logical extension of this, separation of ownership from control does not exist, which means that the controlling shareholders continued to have the management and control power of the company. This may reduce possible principle-agent problems since the controlling shareholder gives the authority to manage the company to an agent who he assigns. In return, the managers may act for the controlling shareholder, but not for all the shareholders. However, in this situation corporate governance issues do more than the agency problems.²⁹ It is difficult to mitigate these problems through conventional corporate governance mechanisms.³⁰ Therefore, at the very beginning, corporate governance principles of Turkey should have aimed at empowering non-controlling shareholders by increasing their occasions to take part in the company management and making the controlling shareholders more accountable to them. In this respect, many regulations such as minority rights, the right to attend the electronic general assembly and receive information, and the right to request a special auditor are included in the reformed TCC. Thus, the early stages of corporate governance in Turkey aimed at ensuring transparency and accountability in order to protect shareholder rights. Naturally, Cadbury's recommendations regarding the social side of corporate governance have also been ignored.

The deviation from the recommendations was mainly due to two reasons. Firstly, the referred OECD principles emerged in states where diverse ownership is dominant. Thus, they focus on how to strengthen individual shareholders against company management instead of protecting minority shareholders from discretionary decisions of controlling ones. This presupposes that the conventional -principle-agent oriented- corporate governance mechanism may not be suitable to be effective for the states where ownership is mostly concentrated.

Secondly, Turkey followed the soft law approach of the OECD principles. This approach is called the 'comply or explain' approach and

²⁸ Demirag, I. & Serter, M. (2003) "Ownership patterns and control in Turkish listed companies" *Corporate Governance: An International Review*, 11(1), 40-51.

²⁹ Tore, I. (2017) "Rethinking agency theory in companies with concentrated ownership" *International Journal of Business and Management Studies*, 9(1), 80-91

³⁰ Fan, J. & Wong, T.J. (2005) "Do external auditors perform a corporate governance role in emerging markets? Evidence from East Asia" *Journal of Accounting Research*, 43(1), 35-72.

characterised by a voluntary implementation of the principles and mandatory disclosure of non-compliance. The implementation of principles was not underpinned by legal sanction. The ‘comply or explain’ approach gives flexibility to companies to decide individually to adopt corporate governance practices according to their specific situations.³¹ However, not having determined any standard for explaining non-compliance created weak corporate governance enforcement. Corporations refrained from implementing particular principles provided that they disclosed some explanation. In addition to that there was not any method to verify the accuracy of these explanations.³² In 2006, the CMB required listed companies to include a Corporate Governance Report in their annual reports. Ararat’s research proved that even though there were around 100 principles, most of the Corporate Governance Reports of companies composed of few pages and was almost the same in the following years.³³ These results indicate that neither the compliance nor the explanation was fulfilled properly.

A question then arises as to whether it is worthwhile for Turkey to adopt the OECD corporate governance principles despite of the differences in ownership structure. The answer is certainly yes, it is. Even though transplantation of the OECD principles did not make a breakthrough change in the corporate culture of Turkish companies, the principles introduced the fundamentals of corporate governance. The vital contribution of implementing the OECD principles was to understand that adequate legal infrastructure is needed to enhance the implementation of the principles. Yet, strict enforcement became necessary for Turkey because for so long time, the soft law approach of the CMB principles were unable to make any significant progress in the business culture of Turkish companies. Consequently, a reformed TCC, which aims to enroot corporate governance to Turkish corporate culture, came into force in 2012.³⁴ In the sense of corporate governance, the primary aim of the TCC is to increase

³¹ Nedelchev, M. (2013) “Good Practices in Corporate Governance: One-Size-Fits-All vs. Comply-or-Explain” 4(6) *International Journal of Business Administration* 75, 77.

³² Ararat, Melsa and Yurtoglu, B. Burcin. (2012) “Sermaye piyasası kurulu’nun ‘kurumsal yönetim’ konulu tebliğleri ile ilgili genel değerlendirme ve yorum” <http://dx.doi.org/10.2139/ssrn.2040376>

³³ Ararat, M. (2011) ‘Comply or explain’ without consequences; The case of Turkey’. In C. A. Mallin (Eds.), *Handbook on international corporate governance* (pp 355-370). Glos, UK: Edward Elgar Publishing

³⁴ See The Preamble of Turkish Commercial Code Law No. 6102
YÜHFD Cilt: XIX Sayı:2 (2022)

transparency and accountability in corporations since the main conflict between the controlling and non-controlling shareholders is on these issues.

‘Comply or explain’ was a journey. At the end of this journey, the Turkish government has responded to fundamental corporate governance concerns via legislation and has seen the transformative effect of the regulation. With regards to corporate governance, Turkey is well underway on transparency and accountability, but there is still way to go in terms of stakeholders. This leads the law makers to the path of sustainability. In order to continue this progress, it is time for the government to raise awareness on corporate sustainability.

A report released by Corporate Knights and Aviva showed that the world’s largest companies are under-reporting sustainability policies and performance. They analysed 6,261 large companies from 47 stock exchanges. Borsa Istanbul (BIST) ranks 26th in the list where in the top 10, there are three emerging exchanges.³⁵ The presence of three emerging exchanges in top 10 shows that sustainability reporting is taking hold in emerging stock exchanges but not in BIST. Knowing that sustainability is one of the significant investment criteria of international investors, the CMB has published a Sustainability Principles Compliance Framework as a continuation of corporate governance principles in October 2020.³⁶ Although the implementation of these principles is voluntary, it is obligatory to report whether they have been implemented or not. This is an important step for public companies in terms of consistent and comparable reporting regarding sustainability. However, by choosing comply or explain approach the legislator has abdicated and left the responsibility of sustainable governance to companies.

The Nexus between Corporate Sustainability and the Turkish Law Why Company Law but Not Environmental Law?

Companies on their own cannot lead themselves to sustainable development but surely, they share an incontestable part of the responsibility with the governments and lawmakers. This makes the

³⁵ Corporate Knights and Aviva (2019) Measuring Sustainability Disclosure Ranking the World’s Stock Exchanges <https://www.aviva.com/content/dam/aviva-corporate/documents/socialpurpose/pdfs/corporate-knights-stock-exchange-ranking-2020.pdf> (accessed on 21.03.2022)

³⁶ SPK, Kurumsal Yönetim Tebliği (II-17.1)’nde Değişiklik Yapılmasına Dair Tebliğ (II-17.1.a) Official Gazette 2. 10.2020 No:31262, See also CMB Sustainability Principles Compliance Framework <https://www.spk.gov.tr/Sayfa/Dosya/1332>

commercial law, which regulates the decision-making in companies, the starting point of the legal research.

In Turkish legal system, TCC is the legal source of company law. It regulates the relations between the company, its decision-making unit and its stakeholders. Yet, a TCC regulation on integrating corporations with sustainability has not been discussed until recently. On 02.06.2022, the lawmaker brought an additional regulation to Article 88 of the TCC and authorized the Sustainability Reporting Standards of Turkey to determine sustainability principles. This regulation is the first regulation in the field of sustainability in the TCC. On the other hand, Article 56 of the Turkish Constitution regulated environmental protection under the social and economic rights and put a positive obligation on the state.³⁷ However, Article 56 does not make specific reference neither to sustainability nor to the responsibility of the companies in this regard. Companies incorporating sustainability into their decision-making do this on voluntary basis.

On the other hand, one can argue that it is indeed the scope of environmental law to regulate the extent to which companies incorporate environmental considerations into their decision-making. Why not environmental law but commercial law should deal with the problem? First of all, environmental law is a set of rules for the protection of the environment. It deals with the issues such as protection of the environment, pollution, decontamination and so on. It has nothing to do with internal regulation or decision-making of a company. Besides, it is out of the scope of the environmental law to keep up with every action of the companies, the possible harm of these actions to the environment and the method of disclosure of these harms to the public.³⁸ Nevertheless, corporate sustainability is a certain way of thinking. It deals with balancing complex environmental concerns with the social and economic interests, which is basically the interest of the managing board in a company. Thus, environmental law would not be the right means to make the company boards to think in this certain way. In addition to environmental law that mandates protection of environment, a company law perspective which will make the company boards to work towards a sustainable corporation is necessary.

³⁷ Turkish Constitution Law No. 2709 Official Gazette 9.11.1982 No: 17863, Article 56

³⁸ Sjäfjell, B. (2010) "If not now, then when?: European company law in a sustainability development perspective" *European Company Law*, 7(5), 187 – 194
YÜHFD Cilt: XIX Sayı:2 (2022)

Even though environmental law and company law are categorised under different branches of law, they could be considered together and in connection with each other to mitigate environmental degradation. This has never been considered as an option in the reformation process of TCC. Obviously, the TCC does not mandate companies to ignore environmental law compliance in order to gain profit. However, this happens in practice in order to maximize shareholder value. This indicates that even a recently reformed commercial law may not be effective enough to lead companies in sustainability and may constitute barriers despite all its novelties on the governance of the companies. Thus, examining the role of Turkish company boards will shed light on the need to translate sustainability into specific legal regulations.

Board of Directors as a Barrier for Sustainable Companies in Turkey

The board of directors (BoDs) under Turkish company law is regarded as one-tier system. According to Article 359 of the TCC, the BoDs of joint-stock companies consist of one or more persons appointed by the articles of association or elected by the general assembly.³⁹ The BoDs are responsible to the company.

In practice, due to the ownership structure of Turkish corporations, the BoDs is mainly composed of the members of the major shareholders.⁴⁰ In another saying, in most of the companies the dominant shareholders happens to be board members. Thus, in many cases the election of board members becomes a formality because the dominant shareholders agree on members in advance and they have the last word. This is to say that the BoDs fiduciary duty is primarily to the controlling shareholders.

Article 375 of the TCC regulates the inalienable powers and duties of the BoDs.⁴¹ Accordingly, it is an inalienable duty of the BoDs to set the corporate governance disclosure and submit it to the general assembly. Even though the TCC was designed to embed corporate governance principles within the Turkish business culture, fundamental principles concerning corporate governance are stated in the Corporate Governance Principles and the related communiqués issued by the CMB. Accordingly, the publication

³⁹ The Republic of Turkey Turkish Commercial Code Law No. 6102 Official Gazette 14/2/2011 No:27846, Article 359

⁴⁰ Eroğlu, M. (2013) "Obstacles and possibilities for sustainable companies in Turkey" University of Oslo Faculty of Law Research Paper No. 2013-04. Retrieved from: <https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2218220>

⁴¹ TCC, n above 39, Article 375

of a corporate governance compliance report in the annual reports is a requirement for listed companies.⁴² Before the publication of the Sustainability Principles Compliance Framework of the CMB, the only sustainability-related principle states that the BoDs should *take all required measures to assure that the organization of the company meets environmental conditions*.⁴³ However, since profit maximization for shareholders is in the heart of corporate governance understanding of Turkey, this principle is in practice ignored.⁴⁴ It is also crucial to mention here that the articles of association of a joint-stock company may deviate from the provisions of the TCC if only this is expressly permitted by the Law.⁴⁵ The TCC lists the mandatory content of articles of associations. Consequently, any provision which is not against mandatory provisions may be included in the company's articles of association. Conclusion that can be drawn from the interpretation of these provisions is that shareholders can hold the BoDs responsible for acting and reporting with an understanding of sustainability by amending the articles of association.⁴⁶ However, the shareholder-oriented logic in addition to the ownership structure of companies have become crucial obstacles for the BoDs to act with an understanding of sustainability in a voluntary way. As the BoDs are dominated by controlling shareholders, they continue to act for the benefits of controlling shareholders, but not for the all stakeholders. As a result, there would be a little room for actions towards sustainable companies.

Due to the concentrated ownership of Turkish companies, minority shareholders have very limited power to influence the management of the company. It would not be wrong to say that this is the case for institutional and foreign investors as well. The absence of organisational behaviour by minority and institutional shareholders is obscuring policy change in the BoDs to act in sustainable ways.

⁴² Kurumsal Yönetim İlkelerinin Belirlenmesine Ve Uygulanmasına İlişkin Tebliğ (Seri: IV, No: 56) Official Gazette: 30.12.2011 No:28158, Article 1

⁴³ Capital Markets Board of Turkey, Corporate Governance Principles Capital Markets Board of Turkey (2003), http://www.cmb.gov.tr/regulations/files/corporate_governance.pdf, Section 2.12.j

⁴⁴ Eroğlu, M., n above 42

⁴⁵ TCC, n above 39, Article 340

⁴⁶ According to Pulaşlı (n above 13) even though there is no provision directly regulating the sustainable company policy and protection of environment standards in the existing TCC, TCC Art. 375/1-e can be applied indirectly for the responsibility of the board of directors.

However, except for the situation occurs between the corporate law and the corporate culture that pose an obstacle to sustainability, Turkey also presents opportunities for sustainable companies. First of all, Turkey is an EU candidate country. Their relation in commercial terms is developing steadily.⁴⁷ The legal reform that started with the EU accession negotiation process has gained momentum with the increase in trade volume. Turkey enacted many laws by following the EU law and still opens up to follow developments taken place in other jurisdictions.

Green Debt Instruments, Sustainable Debt Instruments, Green Lease Certificates and Sustainable Lease Certificates issued by the CMB is an example of the developments in environmental sustainability field.⁴⁸ Within the framework of the 11th Development Plan and the Paris Climate Agreement priorities and actions, a regulatory framework has been drafted to encourage the financing of investments that will contribute positively to environmental sustainability. The aim of green debt instrument and green lease certificate is to provide financing instruments for investments aiming to adapt climate change and to reduce risks arising from climate change and to protect investors financing green projects that can contribute to environmental sustainability, and to increase transparency, accountability, consistency and comparability.⁴⁹ With the Guidelines on Green Debt Instrument and Green Lease Certificate, the CMB has determined the basic principles and minimum standards to be followed in the financing process of green projects. The guidelines has been prepared based on the International Capital Market Association, Green Bond principles. The fact that the reporting process is among the basic components of green debt instruments reveals the importance the legislator attaches to the transparency and accountability of green projects.⁵⁰

Another recent development is the publication of the Sustainability Principles Compliance Communiqué.⁵¹ In order to reinforce the investor confidence, transparency and accountability and to diversify the

⁴⁷ The Republic of Turkey Trade Ministry. (2021, February 18). Yanı başımızdaki dev pazar Avrupa Birliği. <https://ticaret.gov.tr/dis-iliskiler/avrupa-birligi/yani-basimizdaki-dev-pazar-avrupa-birligi> (accessed on 21.03.2022)

⁴⁸ SPK, SPK Yeşil Borçlanma Aracı ve Yeşil Kira Sertifikası Rehberi (Kasım 2021) <<https://www.cmb.gov.tr/Sayfa/Dosya/162>>

⁴⁹ Ibid.

⁵⁰ Ibid

⁵¹ SPK, Kurumsal Yönetim Tebliği'nde Değişiklik Yapılmasına Dair Tebliğ, n above 38.

opportunities that contribute to sustainable companies, the CMB published the principles, the main subject of this study, in September 2020.

A New Step for Sustainability: The CMB Sustainability Principles for Publicly Traded Companies

Investment decisions directed by environmental, social and managerial factors have become a transformative effect on the regulatory institutions and stock exchanges.⁵² In this transformation process, companies are expected to prioritize, adopt and contribute to sustainability and integrate its factors to their operations. They are also expected to undergo periodic performance reporting processes in the field of sustainability. Thus, states which have established norms and standards for corporate sustainability becomes the target of investors since these norms and standards improve transparency and disclosure so that investors can compare the sustainable investment options easily. Thus, sustainability becomes a natural part of corporate governance.

Corporate sustainability being such an important criterion for investors made it inevitable to make legal arrangements. In accordance with the transformation process, the CMB amended the Corporate Governance Communiqué in order to ensure that public companies take concrete steps to ensure sustainability. The amendment entered into force on 2 October 2020. The CMB also published the ‘Sustainability Principles Compliance Framework’, which are the principles publicly held companies are expected to comply with. It is declared that public companies should report their sustainability activities for 2020 in their annual reports to be published in 2021, based on this new set of principles, according to the ‘comply or explain’ approach. Although the compliance of the companies with these principles will be on a voluntary basis, it will be obligatory to report whether these principles are followed and explain in case of non-compliance. The companies will, thus, inform the public about how they comply with the sustainability principles within the scope of their annual reports.

The sustainability principles determined by the CMB are based on three main areas: Environmental Principles, Social Principles and Corporate Governance Principles.⁵³ In this context, it is the duty of the BoDs to determine the priority issues in these areas in order to form company

⁵² Eccles, R.G. & Klimenko, S., n above 14

⁵³ CMB Sustainability Principles Compliance Framework

<https://www.spk.gov.tr/Sayfa/Dosya/1332>

YÜHFD Cilt: XIX Sayı:2 (2022)

policies and announce them to the public. Based on the TCC Article 375, the BoDs are responsible to establish a committee responsible for the implementation of policies in this area.⁵⁴ It is clearly seen that the regulatory body aims to impose duty on the BoDs to create sustainable companies.

The purpose of the amendment is to systematically reduce the risks in order to protect investors and ensure the effective functioning of the market without compromising the ability of future generations to meet their own needs. At this stage, the amendment serves to raise awareness in order to enable companies to formulate policies to add sustainability into their internal processes. However, there is still much room for improvement.

Criticism on the Sustainability Amendment of the CMB Corporate Governance Communiqué

Regulation is a key to achieve sustainability. However, it is not enough to simply throw laws and regulations at a problem. In order to achieve the desired results, laws and regulations must be drafted carefully and evaluated afterwards. Under the Turkish corporate culture where controlling shareholders dominate the boards and focus mainly on profit maximization, the availability of widely applicable regulations on sustainability is especially important. In this context, it is likely that the shortcomings of the amendment will prevent implementation in a widespread manner.

First of all, the CMB follows a soft law approach regarding sustainability implementation instead of putting a stronger emphasis on the hard law characteristics. The advantage of the soft law approach is that it gives companies the opportunity to decide individually to adopt sustainable practices according to their own specific situations.⁵⁵ Besides, such a voluntary approach can lead to less detailed mandatory regulations, thus shuns the lawmakers constantly catching up with developments in companies. However, the previous corporate governance implementation experience of Turkey shows that the ‘comply or explain’ approach has an obvious setback. Owing to the voluntary approach, there is no penalties for non-compliance as long as the reason for non-compliance is explained. The problem arises here is that there is no minimum standard or method to verify the accuracy of explanations. Thus, companies are allowed to decide not to implement the principle, provided that they disclose some sort of explanation. The effectiveness of voluntary approach lies in explanation of non-compliance. This explanation should include justifiable reasons for, as

⁵⁴ TCC, n above 39, Article 375

⁵⁵ Nedelchev, M., n above 33

well as the risks of non-compliance. Without explanation, the voluntary basis does not achieve its purpose at all. As a result, lack of minimum standards for non-compliance and method to verify the accuracy of explanations facilitate the creation of a system, which confers on corporations a degree of immunity from the consequences of incomplete reports.

Secondly, both the CMB Corporate Governance Communiqué and Sustainability Principles Compliance Framework put the responsibility on the BoDs to determine the priority issues, risks and opportunities regarding sustainability, create appropriate policies, prepare reports and disclose them to the public. However, there is no explanation as to how the BoDs will do this. One can declare that as preparing and disclosing corporate governance report is an inalienable duty of the BoDs, sustainability disclosure can be accommodated to this report.⁵⁶ That is to say the corporate governance committee can prepare sustainability report together with corporate governance report. As an opposing view, it can be argued that sustainability requires a separate expertise. The main focus of corporate governance is the internal functioning of the company and its relationship with the shareholders. However, corporate sustainability requires specialities not only on corporate governance but also on environmental problems such as climate crisis, renewable energy and social problems such as employee rights. Consequently, a separate committee responsible for the implementation and disclosure of sustainability policies should be established. Sustainability Principles Compliance Framework advises companies to establish a separate committee.⁵⁷ It is the duty of the BoDs to establish this committee.⁵⁸ At this point, the amendment of TCC Article 88 can be a guideline. It enforces that the Public Oversight, Accounting and Auditing Standards Authority is entitled to determine and publish the Turkish Sustainability Reporting Standards in order to ensure the unity and validity of the reports on sustainability for the businesses and organizations it determines. The article also states that institutions and boards established by law to regulate and supervise certain areas can make detailed regulations regarding the standards that will be valid for their own fields, provided that they comply with the Turkish Sustainability Reporting Standards. However, this new regulation, as can be understood from its wording, has determined the institution authorized to regulate the standards, but does not give

⁵⁶ TCC, n above 39, Article 375

⁵⁷ CMB Sustainability Principles Compliance Framework, n above 55, Section A2.

⁵⁸ TCC, n above 39, Article 366

YÜHFD Cilt: XIX Sayı:2 (2022)

sufficient detail about the formation and competencies of the committee. Therefore, the sustainability committee is regulated in neither the law nor communiqué among the committees established by the BoDs as a mandatory provision. The fact that the establishment of this committee being merely a recommendation in the Sustainability Principles Compliance Framework may cause companies to avoid establishing this committee. To encourage companies to adopt the spirit of the sustainability principles, a more precise regulation would be useful.

Another drawback is that the information foreseen to be shared in the Sustainability Principles Compliance Framework is organized in a very general way. Keeping the classification comprehensive may cause any kind of activity to be named under the heading of sustainability, which would result in greenwashing. This can even be abusive to a certain degree since the legislator does not prescribe any form of reporting and disclosing standard for these activities. In addition, monitoring by minority and institutional investors would not be an effective redress due to their relatively weak position in the company management. There is less developed practice in auditing. The problem lies in the structure of reporting.⁵⁹ Reporting structure of financial reports differs from the annual reports. The annual reports provide explanations of the company's performance. According to the sustainability amendment of the CMB, sustainability reports will be included in annual reports of the companies.⁶⁰ However, Turkish Accounting and Auditing Standards, which is compatible with international standards, has largely concentrated on financial reporting. The point of view can be better understood with the statement of van Mourik (2011); '*All the IASB board members share the same positivist ontology focusing on accounting as a technical tool aimed at faithfully representing an entity's financial reality, rather than as a social construct which generates intended and unintended economic, social and environmental consequences.*'⁶¹ It should also be remembered that auditing

⁵⁹ Villiers, C. & Mähönen, J.(2015) "Accounting, auditing, and reporting: supporting or obstructing the sustainable companies objective?" in Sjäfjell, B. & Richardson, B.J. (Eds.), *Company law and sustainability: Legal barriers and opportunities* (pp. 175-225). Cambridge, UK: Cambridge University Press.

⁶⁰ SPK, Kurumsal Yönetim Tebliği'nde Değişiklik Yapılmasına Dair Tebliğ, n above 38, Article 2

⁶¹ Van Mourik, C. (2011), "Response to the IFRS Foundation's Report of the Trustees' Strategy Review"

is retrospective.⁶² However, sustainability is about the interpretation of the future. The important thing at this point is to identify environmental and social hazards as well as economic ones while they are still preventable and inform the BoDs about these potential dangers so that the board can take timely measures. As it can be seen, determining sustainability policies and reporting the activities require a different approach and expertise than financial reporting. The International Integrated Reporting Council had published a globally accepted framework for sustainability reporting. However, integrated reporting is still in its development stage in Turkey and a standardization on integrated reporting is needed urgently.⁶³

Complementary Reform Proposals

Based on the discussions briefly set out above, in order to achieve corporate sustainability through legal regulations in Turkish companies 3 main points need to be addressed; reformulating the purpose of the company with regards to the necessity of regulation in terms of sustainability, the role of the BoDs and determining concrete practices for the implementation of advised sustainability compliance principles, such as determining reporting standards and legal sanction.

a. Redefining the Purpose of Companies

One of the discussions on corporate sustainability is about whether there is a need for a legal necessity on this matter. Since companies' first and foremost aim is to gain profit, one can state that corporate sustainability should be based on volunteer basis. Additionally, Turkish commercial law gives capability to the BoDs to shift onto a sustainable path voluntarily. However, due to the increasing importance of the issue for investors, sustainability should not be left to the free will of the companies. Especially in emerging markets such as Turkey, leaving the issue to the free will of companies may prevent sustainability from becoming widespread among companies. Thus, firmer rules that lead the BoDs towards sustainability is needed. Broadening the scope of corporate governance with sustainability will provide a redefined room for the creation of economic value, with ample space for environmental and social value, and enable businesses to reach a higher level of transparency on these matters. As Turkey is far off track from corporate sustainability, what urgently needed is to accept that environmental and social degradation will sooner or later affect the

⁶² The Preamble of the TCC, n above 36, Article 378

⁶³ Ercan, C. & Kestane, A. (2017) "Entegre raporlama ve Türkiye'deki uygulama örnekleri üzerine bir araştırma" *Kırklareli Üniversitesi İktisadi ve İdari Bilimler Fakültesi Dergisi*, 6(4), 73 – 86.

commercial life. Thus, going beyond the traditional purpose of the company and clarifying that profit should be achieved within the overarching goal of sustainability is the first step the legislator can take to raise awareness.⁶⁴ To this end, the purpose of companies should be defined, for example in TCC, as ‘*The purpose of a company is to create sustainable environmental, social and economic value while respecting the interests of its investors and other stakeholders.*’ This definition should be supported by detailed legal regulations for different types of companies. Only after such a redefinition will the CMB sustainability principles be interpreted and implemented eloquently.

b. The Role of the BoDs

Redefining the purpose of company will not reach to any change in reaching a level of sustainability in companies unless it is integrated into the duties of the BoDs. The BoDs have vital part to play in the evolution of sustainable companies. As a consequence of economic progress and increase in competition, the traditional ownership structure of companies has begun to change. Today, the BoDs must serve the interests of all stakeholders, not just the interests of the founding shareholders.⁶⁵ Pashl stated that one of the most important differences between corporate governance and traditional management is the implementation of “rules” and “discretion”. In its broadest sense, corporate governance is a system that includes rules regarding shareholders and stakeholders. Accordingly, it is the duty of BoDs to determine the core strategies that concern all the stakeholders. This view is also supported in the European Commission by stating that it is the BoDs who determines core strategies and integrate social, environmental, human rights and stakeholder concerns into these strategies with the aim of maximising the creation of shared value for their shareholders and other stakeholders and society at large; and identifying, preventing and mitigating their possible adverse impacts.⁶⁶ The OECD also supports such a formulation of the duties of the BoDs.⁶⁷ Therefore, at the TCC level, the duties of the BoDs should be reformulated and a clause such as ‘*to ensure the creation of sustainable value*’ should be added to Article

⁶⁴ Willard, B. (2014) “Better is not good enough: Toward true corporate sustainability” <https://greattransition.org/publication/better-is-not-good-enough> (Accessed on 20.03.2021)

⁶⁵ Pashl, A. (2004). *Anonim ortaklık kurumsal yönetimi*. İstanbul: Beta.

⁶⁶ European Commission, Green Paper The EU corporate governance framework <https://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2011:0164:FIN:EN:PDF>

⁶⁷ OECD, OECD Guidelines for Multinational Enterprises (2011), <http://www.oecd.org/corporate/mne/48004323.pdf> at 42-46.

375. Thus, the duties of the BoDs regarding sustainability would cover not only reporting but also preparing the sustainability plan of the company. Consequently, such a clause can prevent the BoDs to see sustainability as only a duty of reporting. This clause should be undergirded by detailing the Sustainability Principles Compliance Framework on the possible content of the plan, objectives to be achieved and key performance indicators for impacts that are relevant. Although the Compliance Framework is not mandatory, such a detailing will guide companies on how to prepare the plan. This will lead to reach a standardization which will contribute to not only lowering costs, but also augmenting transparency of the companies. In this way, investors can check at regular intervals to what extent the companies comply with the plan. In summary, ensuring sustainability should be among the inalienable duties of the BoDs as a mandatory provision. The standards recommended within the Compliance Framework should be of a guiding nature to the BoDs and should not burden the companies excessively.

c. Reporting and Auditing

Conventional accounting with its focus on the measurement, calculation and valuation of financial assets and profits primarily serves the interests of the companies and their shareholders.⁶⁸ Complementarily, transparency understanding of the profit-oriented corporate governance is based on disclosure of financial assets and profits. In another saying, it is about sharing accurate, sufficient, timely and comparable financial information regarding the company's financial situation and performance.⁶⁹ The foregoing dynamic of the wealth creation had nothing to do with non-financial disclosure.⁷⁰ Thus, activities which remain unmeasured are disregarded to be disclosed.

Under Turkish law, regulations for financial information disclosure are found in both TCC and CML. However, for non-financial information, voluntary disclosure has been determined. There is no direct binding regulation on this regard. A criticism against the new amendment requiring companies to disclose sustainability principles compliance has been that the reporting requirements are not based on a clear legal duty. Combined with a lack of proper enforcement, when companies are not binded by the law to

⁶⁸ Jones, M.J. (2010) "Accounting for the environment: towards a theoretical perspective for environmental accounting and reporting", *Accounting Forum*, 34(2), 123-138.

⁶⁹ Pash, A., n above 67.

⁷⁰ Li, M. (2009) "Capitalism, climate change and the transition to sustainability: Alternative scenarios for the US, China and the world", *Development and Change*, 40(6), 1039-1061.
YÜHFD Cilt: XIX Sayı:2 (2022)

integrate sustainability concerns into their disclosure policy, there is a risk that disclosure on sustainability becomes neither relevant nor reliable. The amendment foresees that the annual reports of public companies should provide either information regarding whether the sustainability principles are applied, or a comprehensive explanation on the impacts that can be occurred in the environmental and social areas due to the failure of fully compliance with these principles. For the comply or explain approach to be satisfactory, as a first step, the law-maker should give a clear guidelines on disclosure of environmental and social information. Considering the facts that Turkey's accounting standards are compatible with the EU, it can be advised to take the guidelines the European Commission in relation to the non-financial reporting as a model.⁷¹ As a second step, it would be a deterrent factor to impose sanctions on inaccurate or non-explanation. The Communiqué specifies general framework that will be disclosed. However, no provision is regulated regarding the sanctions the company will be imposed if the required information is not disclosed. To make the companies disclose correct and accurate information on time, it would be appropriate to envisage sanction.

Sustainability disclosure in publicly held companies is a fundamental step which leads us to another issue; how will the accuracy of the information provided in the annual reports be verified? Sustainability assurance is not obligated by the communiqué. However, it is stated that sustainability performance measurements must be disclosed after verified by independent sustainability assurance providers. In other words, the authority in checking the accuracy is left to the auditors. At this point, the expertise and competence of the auditors regarding sustainability management processes and explanations will come to the fore. It is obvious that sustainability assurance auditing is not as common as financial statement auditing. It is stated that legal basis of this situation are; lack of national regulations, lack of knowledge on international standards, lack of legal obligation for assurance auditing. In the absence of national regulation, providing supervision and guidance services by competent authorities will be a solution that will facilitate the reporting process.⁷² Actually, it would be ideal to regulate sustainability reporting and assurance from the very beginning in order to refrain from a patchwork of regulations. However,

⁷¹ The EU NFRD, n above 23

⁷² Atabay, E. (2019) "Kurumsal sürdürülebilirlik raporları ve güvence denetimi: Türkiye'de GRI rehberine göre raporlama yapan firmalar üzerinde bir araştırma", *Muhasebe Bilim Dünyası Dergisi*, 21(4), 904-922

given that even the amendment is a big step, these shortcomings can be rectified with subsequent reforms.

It should also be indicated that Sustainability Index created by BIST is an extremely important incentive for public companies for the development of sustainable reporting. The purpose of the BIST Sustainability Index is to create an index in which companies that have high corporate sustainability performances will take place, thus, increase practice of sustainability among companies in Turkey. In order for the companies to be listed in the index, there is no requirement to publish a sustainability report. However, companies must pass the threshold values in the "Index Selection Criteria". As of the end of September 2018, there were 44 companies in the Index. At the end of April 2020, this number increased to 61. It is clear that making legal arrangements and providing incentive mechanisms by BIST support the developments in this area. In the long-run, it can be advised to convert soft law approach of compliance and reporting to binding law.

In summary, with the amendment sustainability principles were determined. These principles were added to the Corporate Governance Communiqué of the CMB and the compliance framework was prescribed by the legislator as a soft law. The next step should be to spread the implementation with the incentives of BIST and other related organizations such as Integrated Reporting Network Turkey and the Turkish Industry and Business Association. Ultimately, what is now applied on a comply-or-explain basis should be mandated.

Concluding Remarks

If sustainability is desired as a society, companies must be part of the solution. The increasing importance of the role of companies in sustainability foretells a new perspective of corporate governance norms and practice. This is because even though it is not required as a matter of law, sustainability is stymied by the shareholder oriented approach of corporate governance. But sustainability, being among the investment criteria of many investors, has educed that sustainable corporate practices prove profitable. As a consequence, in order to attract investors, any regulation in law which slow the progress of corporate sustainability should be amended.

This article provides an overview of Turkish corporate governance and its relationship to corporate sustainability. It seeks to reveal the barriers to corporate sustainability and offers complementary reform proposals. The root of the barriers is the commonly held view that companies must strive to maximize shareholder profit at the expense of everything. This view imposes a formidable obstacle to corporations to become sustainable. This

view together with the corporate ownership structure of Turkish companies gave impetus to BoDs to fulfill their fiduciary duty primarily to the controlling shareholders. This common misconception led to sacrifice stakeholder benefit to profits. The implementation of corporate governance principles did not change this situation. Because companies are not willing to compromise their freedom, the method of ‘comply or explain’ in the current corporate culture did not reach the desired efficiency. Since companies did not do enough on a voluntary basis, it became inevitable for the legislator to take concrete steps in this regard. Thus, Sustainability Amendment of Corporate Governance Communiqué came into force in October 2020.

The amendment is beneficial, insofar as it sets out a ground in terms of sustainability that could feature as a starting point in legislative initiatives. Considering the past experiences of Turkish companies with corporate governance, it can be stated that the amendment on its own will not be effective enough to lead companies in sustainability. In order for a better compliance, further amendments are needed. In this regard, first of all sustainability should be one of the key purposes in the definition of companies as a matter of company law. Thus, society can find the legal basis to demand for changes in terms of sustainable companies. Assisting the redefinition of the company, creation of sustainable value should be integrated into the duties of the BoDs in the TCC. Assigning a more comprehensive duty on the BoDs will hold them liable for not only reporting but also establishing a separate sustainability committee, preparing sustainable business plan, disclosing accurate and adequate explanation and so on. Lastly, sustainability disclosure requirements are strikingly insufficient. Disclosure is left to voluntary measures. Even though the amendment is a good initiative, much effort is needed especially on verifying the accuracy of explanation. In addition, there is no requirement on reporting and auditing of environmental and social information. This leads to risk of lack of comparability and consistency which would result in uncertainty in benchmarking. National regulation on the reporting and auditing sustainability practices of companies, such as mandatory integrated reporting, is needed urgently.

Voluntary implementation can be spread by encouraging companies to sustainability in various ways. BIST-Sustainability index is one of the good incentives. Investors know that the sustainability activities of the companies listed in the index are at a certain level and they invest accordingly. Reduction in the listing fees for the companies included in the index can be

an incentive to increase the number of listed companies. In the future, special incentives for family businesses, non-public companies and different sectors may be considered.

Sustainability being an investment criteria has made it inevitable for international policy makers to make regulations in this area. Sustainability research in Turkey is in an embryonic stage. Thus, the literature lacks a comprehensive and systematic understanding of this emergent body of inquiry and a holistic agenda for empirical research. Despite its exploratory nature, the insights gained from this study may be of assistance to understand the key areas to be improved drawing on the lessons learnt from the past. Recalling that corporate governance principles are a living instrument, it is expected that means for consolidating corporate sustainability via corporate governance will emerge over time. Future research should examine the annual reports of listed companies to explore how the new set of principles is reflected in the market by analysing the reaction of investors; whether complied or explained in a reliable, relevant and comparable manner; whether much harder law is needed.

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