Sustainable Transformation of Business and Finance

A democratic challenge in an age of climate change and artificial intelligence

2023 McGill SGI Academy Impact Paper

1 June 2023

Presented by the
2023 McGill SGI Transformative Business Law Summer Academy
McGill University

McGill UNIVERSITY | Faculty of Law | Faculté de Droit | Sustainable Growth Initiative

DESAUTELS

UNIVERSITY OF AMSTERDAM

Abstract:

Corporations are among the dominant contributors to climate change and environmental degradation. At the same time, they could still become champions to turn the ship around. With great power comes great responsibility. The emphasis on profit maximization led carbon majors to be one of the main contributors to climate change. Additionally, globalized and multi-level production and trade have led to concerns for human rights in business processes. Furthermore, the inaction of big techs in addressing mis/disinformation in their platforms has led artificial intelligence to destabilize democratic discourses.

The planetary crisis, modern slavery, and democratic erosion propelled Academy fellows and faculty to respond with urgency.

As the TBLSA Impact Paper puts forth, business law and finance offer effective avenues, such as the purpose-driven business model and the revaluation of asset management, for a just transition which takes into account climate justice, more meaningful transparency, and algorithm accountability so long as public and private actors implement the concrete policy recommendations proposed in this brief.

Key words:

Climate change; sustainability; artificial intelligence; algorithm governance; democratic crisis; carbon majors; asset managers; planetary crisis; climate justice; and just transition.

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Foreword

By Simon Archer and Peer Zumbansen

The McGill SGI Summer Academy of Transformative Business Law came together in Montreal in May 2023 to address the multifaceted challenges that confront governments, business, and civil society actors in a context for which the clock has been ticking. The participating Fellows came from Brazil, Colombia, China, the U.S., Canada, France, Germany, and the Netherlands, to name just a few. They came to work 12-14 hours a day to explore, to question, and to analyze the existing conditions and obstacles in the way of transformative change. They brought their expertise in law, business, management, anthropology, environmental studies, economics, accounting, and political theory to shine a bright light on the present and how we got here. They displayed a keen awareness of the contrast between short-termism and profit maximization on the one hand and the increasingly vacuous phraseology of 'global citizenship' on the other, coming at a time when fewer "have" and many more "have not."

Over the course of a few days, they were accompanied and advised by an equally interdisciplinary and international cohort of Academy Faculty. The Academy has been geared towards the elaboration of concise and to-the-point analysis pieces on a range of the most pressing contemporary political, economic, legal, and cultural challenges. They worked together in learning how to cut through the noise, distinguish between the polemic and the genuine, between truth and chatter.

The inaugural 2023 Academy met with a sense of urgency. It has sought to bring together a number of key insights into the contemporary constellation in order to formulate what the Academy members hope to be constructive as well as inspiring, if sometimes provocative, suggestions of how to take steps towards transformative economic and societal practices. The Academy's findings and recommendations are documented in this 2023 Impact Paper, which was launched on June 1st, 2023, on the Academy website

(https://www.mcgill.ca/business-law/). Simultaneously, the Academy posted a video documentary trailer on the work of the Academy on its website and on Youtube (https://youtu.be/zNiNkLTNmFk). The Academy is an annually recurring event and is convened in the hope to foster constructive and inclusive collaboration towards the elaboration of usable, pragmatic, and critical insights into the challenges of our time.

As the Report was written, we were again witnessing another sobering illustration of what the legal anthropologist Eve Darian-Smith calls *Global Burning*. Quite literally, wildfires were out of control near Halifax, Nova Scotia, one example of Darian-Smith's constellation of planetary deterioration through wildfires, floods, and earthquakes. Politically, election after election confirms the sobering trend towards authoritarian and populist politics and discourse. Authoritarian leader Recep Erdoğan was re-elected President of Turkey on the second day of the Academy, extending his rule beyond 20 years, while, in Canada, the outcome of Alberta's provincial election might pit the province, home to the world's third-largest oil reserves, on a conflictual course with the federal government's carbon emissions and clean electricity strategies.

As around the world climate change regulations, diversity-, inclusiveness- and ESG- ("*environmental, social* and *governance*") informed corporate governance and finance reforms are becoming battlegrounds for political confrontation, democracies are being put to a test. Today it is hard to ignore that the dreams of past decades of addressing planetary challenges – from poverty and hunger to migration, security, and inequality – through emerging infrastructures of global governance have been displaced by surging nationalism and an explicit discontent with a largely economic drive for globalization that can no longer be ignored. Examples of outright conflict, radicalization, and polarization abound, and the political "Overton window" for immediate and impactful responses to climate and other pressing social concerns seem to grow smaller each week.

The climate crisis today exposes a number of frightening if not debilitating facts. Not only does it challenge prevailing assumptions regarding growth and progress, but it also lays

bare the exploitative and destructive dynamics of how the affluent relate to, benefit from, and discriminate against those that are vulnerable. Climate change prompts us to confront, globally, the unequal relationship between takers and users, and between makers and impacted, to pick up on pertinent observations made by the Financial Times's Rana Foroohar a few years ago. We are past due in recognizing the injustice that what Ulrich Brand and Markus Wissen call the "Imperial Mode of Living," an unsustainable relationship of taking, not giving, of exploiting instead of collaborating and empowering. The U.S. American social theorist Nancy Fraser, a long-time thinker about the infrastructures and values of welfare state regimes, has coined this constellation between the haves and the exploited, extracted, and suppressed ones "Cannibal Capitalism." She joins those across political science, sociology, anthropology, economic geography, labour economics and law, and political economy who have been tirelessly exposing the detrimental and ultimately destructive effects on the current way of life on humanity and the environment.

What is the role here of governments, businesses, civil society actors, and educational institutions? How can collective action be reinvigorated towards a transformative engagement with the most pressing challenges we all face - together, on a planetary scale? In an era where elections in a region with faltering health care and shrinking public services are won with historically low voter participation on the promise of 'carry on', in an era where governmental leaders in those parts of the world with the largest GHG emission footprint vow in a populist gesture to defeat any climate change mitigation efforts, how are we to hope that the next generation does not simply turn inward and away from the vile, the noisy, the hostile? How can we look the surging post-pandemic mental health crisis in the eye and not despair over the shrinking spaces of innovative and transformative and, crucially, inclusive and empowering action?

Is there any role left for the University? How can it work better with civil society actors, with policymakers, and industry partners? How can it enhance a collaborative

engagement in educating tomorrow's leaders to do things differently, to turn the ship around, to be brave to ask the tough questions and to be even more courageous and tenacious to insist on the answers and their implementation? The Academy is but a small, small part in what is a much larger, global conversation and a collective undertaking. It is an honor to work with brilliant and alert students and colleagues far beyond the University in contributing to this effort.

Simon Archer, Peer Zumbansen

Montréal, 1 June 2023

Executive Summary

The inaugural Academy of Transformative Business Law came together in Montreal in May 2023 to address the multifaceted challenges that confront governments, business and civil society actors with a sense of urgency. The participating Fellows from Brazil, Colombia, China, the U.S., the UK, Ireland, Canada, France, Germany, and the Netherlands, to name just a few, explored, questioned and analyzed the existing conditions and obstacles in the way of transformative change.

Applying their expertise in law, business, management, anthropology, environmental studies, economics, accounting and political theory to shine a bright light on the present and how we got here, they formulated a number of constructive and practice-oriented recommendations. These and the analysis that supports them displays a keen awareness of contemporary short-term thinking and the myopic, seemingly undeterred focus on profit maximization. The collaborative, interdisciplinary and inclusive process that shaped the Academy's recommendations is meant to make a small contribution to what must be a global conversation and call to action. The Academy's initial coming-together and its findings add to the efforts among those who call out the disconnect between those who are responsible for climate change and those who have been and will be most affected by it.

Accompanied and advised by an equally interdisciplinary and international cohort of Academy Faculty, the Fellows set out to map and explore some of the most pressing contemporary political, economic, legal and cultural challenges in confronting the climate crisis. With a focus on how modern businesses continue to be run, their work focused on the promises and the contestable variations in implementing robust corporate governance changes towards an institutional practice geared to ESG, diversity and inclusivity. The Academy's work explored the multi-tiered and historically entrenched system of financing through debt and equity, locally,

nationally, globally from the perspective of how to achieve a forward-looking regime of sustainable finance, especially with regards to building a more robust system of green investments, on the one hand, and reflecting on the role of old-age security/pension funds as shareholders, on the other. The Academy explored the challenges of understanding and conceptualizing, proceduralizing and implementing what must be a comprehensive, all-transforming law, economics and politics of climate change governance. The organization of global financial and economic exchanges requires the acknowledgement of the key role played by global value chains and their constituting role in organizing and structuring real-world opportunities of access and participation but also of extraction and exploitation.

The technological innovations that have been keeping humanity on their toes since the invention of the wheel, of electricity or DNA analysis continue to transform every aspect of human life, including how we speak to each other, how we discriminate and decide, and how control can become all-encompassing surveillance and suppression. The radical emergence and deepening of artificial intelligence are thus far the toughest challenge of our self-understanding of who we are, how we exist and how we act. Within months the entire world has learned that they may never again need to write a text on their own, look up sources, let alone read them, as they may instead prompt an AI to answer any question they may think of. The shrinking of time horizons in the context of what AI does and what it seems to signify is nothing short of overwhelming. We would be foolish to brush it off or to think that a slogan such as "move fast and break things" is even remotely apt to explain the challenge that AI and those who possess the largest AI-create-and-use capability pose to the survival of democratic, collective and inclusive life.

The Academy Fellows came together to propose what they hope to be constructive as well as inspiring, if sometimes provocative, suggestions of how to take steps towards a transformative societal

practice. The Academy's findings and recommendations are documented in this inaugural 2023 Academy Impact Paper. The Paper was launched on June 1st, 2023 on the Academy website (https://www.mcgill.ca/business-law/) and is accompanied by a video documentary trailer on the work of the Academy on its website and on Youtube (https://youtu.be/zNiNkLTNmFk). The Academy is an annually recurring event and is convened in the hope to foster constructive and inclusive collaboration towards the elaboration of usable, pragmatic and critical insights into the challenges of our time.

The Findings

Ch. I - A Purpose Corporation for a Purpose Economy

The acronym "ESG" currently captures the quest for a corporate purpose or purposes focused on a "greener, sustainable economy, community impact, and diverse boards." But ESG is also symptomatic of a wider discontent with the exclusion of those concerns in corporate decision-making. There are persisting – and deepening – gaps between those who benefit from market returns and those who are striving to assert even minimal agency in shaping their and their dependents' lives.

Today, this is set against a dramatic level of climate change and democracy in crisis. The discontented call for the corporation to redefine its "purpose" – the reason it exists and the role it plays in society and across value chains.

What is needed is more clarity; more open, informed and inclusive dialogue; a discussion of a common vision of the purpose of the corporation and the wider economy; and a broad commitment to work collectively towards meaningful change.

The debate over corporate purpose and responsibility is not new. Its key concerns – value creation for shareholders, and the balance with, inter alia, workers' rights, environmental impacts, taxation and subsidies, assumption of societal responsibility and public functions (social

security, services, infrastructure, R&D, communication and warfare) – have always been public ones. More recently, the slogan of 'corporate purpose' again became the focus of debate in corporate law circles and well beyond through the August 2019 Business Roundtable "Manifesto" in the U.S.

The Academy Working Group focused on the promises and remaining pitfalls of effectively moving business and finance, including corporate governance, towards an impactful, sustainable practice. At the core of the Academy Working Group's proposition is the conviction that if a corporation is to survive and flourish throughout the 21st Century it must address the urgent need to differently balance and relate its profit and its social purposes in society.

Firstly, a corporation must recognize the need to expand its core mission and assess whether the implementation of every one of its actions achieves the purpose-driven objective. The Academy Working Group argues that not only is such a purpose-driven statement needed (whether imposed or voluntary) but that corporations must then be evaluated upon and rewarded or punished for how they achieve this purpose-driven objective, all with concrete, impactful, and measurable changes.

What is needed is for businesses, including start-ups and conventional businesses, to adopt a social purpose as the reason they exist, and then to harness their assets, resources, relationships, and influence, reach, and scale to bring their purpose to life. Social purpose business is defined as a business whose reason for being is to create a better world.

This is the purpose economy. To mobilize stakeholders in the corporation and the economy, they need to be educated about social purpose business, the business case for it, case studies of social purpose business in action, and then tools, guidelines, and standards to formalize and embed social purpose within their sphere of influence. Governments need to adopt policy measures to create this favourable environment for social purpose

businesses to start, transition, thrive, and grow.

Among the Academy Working Group's proposals are the creation of a legal requirement for a social purpose statement to be included in a corporation's by-laws, the implementation of mechanisms to increase stakeholder transparency (e.g., by creating and publishing industry-specific universal ESG metrics; the amendment of prevailing risk assessment practices to more explicitly factor in ESG matters in investment decisions assessments by giving weight to ESG factors when weighing the risk of an investment; the creation of targeted investment vehicles that favour and proliferate socially responsible investment and the amendment of taxation systems to develop a special tax status targeted to reward organizations that meet an ESG-related standard throughout their business practices.

Ch. II - Toward Sustainable Finance

A purpose economy needs sustainable finance. This simple fact is gaining recognition but is not yet systemic in the financial system. At the present time, financial sector actors voluntarily adopt a transition toward sustainable finance, and it is no longer self-evident that financial markets, alone and without support and guidance, will be able to address current challenges in an adequate manner.

When in 1992, James Carvill, the chief strategist for Bill Clinton's presidential campaign, used the phrase that, 'It's the economy, stupid,' what he really depicted was an economy that had undergone dramatic changes since at least one and a half decades before. What had marked public policy since the late 1970s and early 1980s were dramatic shifts away from public expenditures and state-engineered industrial policies towards the liberalization and expansion of financial markets. The decision by the US government in 1974 to allow old age security (pensions) to become tradeable on securities markets through the adoption of the Employment Retirement Income Security Act, marked a watershed

moment in the wide-ranging financialization – that is, the integration of public goods, services and, by consequence, entitlements into the stock market – of the economy. The history of the next 50 years during which almost everything became a tradeable asset forms the backdrop for our inquiry today into the prospects of using financial markets to bring about a 'green economy.'

This section of our Report focuses on 'sustainable finance' (SF) not only as a field of immensely rich and diverse activity but also as an enormously ambitious normative proposal. At the core of this proposal is the assumption that it will or should be possible that financial markets may be able to effectively mitigate or prevent climate change. A closer investigation into this ambitious claim reveals a number of challenges – these include the difficulty in identifying the most suitable actors who should be in charge of assuming roles of agency, intervention, and more. Other challenges are concerned with the identification of and the choice among different policy options.

Canada is perhaps seven years behind other jurisdictions in recognizing the need for a system of sustainable finance, and providing the guidance and incentives to make it a reality. ESG-driven financial regulatory initiatives in Europe far exceed our own.

The Academy Working Group has identified a series of recommendations to help guide the Canadian financial sector to become a sustainable financial system or a system of sustainable finance.

It suggests the protection of large institutional investors in making bold (but prudent) decisions to green their portfolios, while at the same time providing incentives to guide investment in green technologies and products. It identifies the problem with diverse ESG standards and reporting - leading to greenwashing - and makes suggestions to address these problems. Finally, it identifies ways to create "sustainable finance champions" within the wide and diverse actors in the Canadian financial system, from public finance entities to

private financial actors to the regulators who oversee them.

Ch. III - Climate Change changes Everything

Climate change changes everything, as Naomi Klein would have it. Klein argues that the climate crisis requires abandoning dominant liberal market ideologies, restructuring the globalised economy, and remaking political institutions. Taking the iconic catchphrase as its starting point, the Academy Working Group 3 mapped the legal, political, and governance challenges associated with climate change as a prerequisite for the elaboration of actionable recommendations.

The challenge in identifying concrete, ambitious and yet realistic steps towards the wholesome implementation of effective climate change mitigation policies is manifold. It presents itself not only as a regulatory but also as a cognitive problem. As for the question of designing and implementing reliable regulatory instruments, climate change in its ubiquitous effects and origins suggests a multitiered, comprehensive political, regulatory and societal intervention. In that respect, it resembles other complex historical challenges that humanity has struggled with for time immemorial, including poverty, inequality, hunger, and war. As regards our understanding of climate change as a condition that is fundamentally caused by actions as well as inaction that both result from existing and prevailing biases and assumptions, we are confronted with a radical cognitive problem. The perseverance of narratives around 'progress,' 'growth,' and even 'civilization' stands in stark contrast to the enduring legacy of these problems. Climate change must be understood as intensifying and exaggerating this constellation. In its enormity, climate change embarrasses habitual modes of thinking in terms of cause and effect by forcing a much more radical understanding of the same.

The trouble is that climate change does not only change everything; climate change is everything. It is baked into modern economic, financial, and

governance systems, which, under the pretense that unlimited economic growth was possible, incentivize material overconsumption in developed countries while exploiting people, places, and non-human beings predominantly in developing and first-nation communities. It is perpetrated by non-sustainable practices of organizing decision-making processes. These too often remain driven by an unfounded confidence that adjustments or even course reversals in the form of 'tough choices' can wait 'for another day.' Calculating rationales like the 'discount rate' through which we aim at accounting for present-day expenses in exchange for tomorrow's benefits tend to be defeated in the name of the allegedly unacceptable burden these costs would today place on consumers and others.

Turning to climate change as a prompt for a comprehensive transformation of the way in which we see the world and relate to it is also political. It requires public and private actors to work together and negotiate differences across inter- and transnational, national, and local levels. The task is to find not only forward-looking 'solutions' – be they technological or otherwise – but also to acknowledge and provide meaningful reparations for past and future losses and damages. In this sense, climate change is, at the core, a moral issue, a matter of choice, laying bare persisting questions of justice which challenge us across historical, distributive, and epistemic registers.

Ch. IV - Why Global Value Chains Require Our Attention

The on-the-ground day-to-day reality faced by workers in global value chains continues to be appalling, despite the dawn of a new era of human rights and modern slavery laws. Transparency regulations, human rights, due diligence laws, and attempts to establish the civil liability of lead firms have proven ineffective in addressing severe forms of human exploitation, such as child labour, modern slavery, and deplorable working conditions. International and national regulators have persisted with the same approaches, revealing their reluctance to genuinely transform the current methods of global production.

The continuing dominance of certain major firms accused of human rights violations, particularly in sectors such as pharmaceuticals and natural resource extraction, serves as evidence that little progress has been made since the adoption of the [Declaration on the Establishment of a New International Economic Order]() by the UN General Assembly in 1974. Among other things, this declaration called for the "[r]egulation and supervision of the activities of transnational corporations by taking measures in the interest of the national economies of the countries where such transnational corporations operate on the basis of the full sovereignty of those countries."

Consequently, to eradicate modern slavery and other human rights violations in global value chains, we must break free from the regulatory inertia that parliaments, courts, and international organisations have been trapped in and radically change directions. Above all, this necessitates exposing the hidden realities concealed by global value chains and the superficial veneer provided by trendy concepts like Environmental, Social, and Governance (ESG) and Corporate Social Responsibility (CSR). Regulatory responses to this reality must center marginalised voices and acknowledge the physical and emotional suffering that workers and communities endure within these value chains.

In this chapter, we outline a multi-faceted strategy to encourage responsible corporate citizenship by regulators. We highlight the potential for regulators to leverage digital technologies, such as blockchains, to mandate traceability and ensure visibility of the human suffering present within global value chains to consumers and investors. It is equally crucial for regulators to facilitate access to justice for victims of corporate misconduct, irrespective of their location or the timing of their claims. Ultimately, we emphasize that a cohesive and integrated approach that encompasses these recommendations is necessary to break free from the long-standing regulatory

inertia that has failed to yield significant tangible outcomes on the ground.

To that aim, in Chapter 4, the Academy recommends, first, that regulators mandate value chain visibility by making the adoption of blockchains compulsory in order to improve traceability within global value chains. Second, government regulators must consult foreign actors, such as trade unions and local human rights NGOs, when drafting legislation and considering the governance of global chains. In order to address the harms made visible, we suggest the introduction of specific legal mechanisms to lower the barriers that affected third parties face when seeking legal remedies in state courts.

Concretely, this requires states to extend standing in civil suits and to reverse the burden of proof to the benefit of a presumption of responsibility. As a complement to the stick approach of legal liability with incentives for businesses to comply with international human rights standards, we recommend that regulators and NGOs co-create a certification tied to financial incentives, recognising companies do not use slave labour in their supply chains. Lastly, it is clear from attempts to design solutions to the persistence of modern slavery in GVCs, that no one solution on its own is sufficient. Efforts have been made to improve visibility and monitoring, but these interventions have been piecemeal and mostly voluntary. There have been attempts to design new laws, but these have had significant limitations. Incentives have been effective in certain limited cases but not strong enough to drive systemic change.

Finally, the voices of those most affected have long been excluded from the debate and have lacked the major social influence required to drive change. The shortcoming of these approaches, then, is not that they are entirely ineffective but rather they cannot work in isolation. Coherence between these interventions in the form of a coordinated and multifaceted approach is thus absolutely critical if any of these

are to truly address human rights abuses in global value chains.

Ch. V - Can Democracies Survive in the Digital Sphere?

To address regulatory gaps while seeking to uphold principles of democracy and social responsibility, the Academy has looked to 'Very Large Online Platforms' (VLOPs) use of AI systems and the algorithms they use to curate, amplify, and moderate divisive, polarizing content. Regulatory frameworks for corporate social responsibility must include considerations about VLOPs' use of algorithms and AI systems because VLOPs are digital public spheres where political opinions are formed, and thus they form the bedrock of social, economic, and political stability in the country.

The Academy Working Group has drafted policy recommendations that move towards the goal of holding clearly identified creators, controllers, and owners of artificial intelligence systems to account. To do so, the Academy outlines four categories of policy recommendations: 1) accountability measures; 2) transparency measures; 3) responsibility-by-design measures; and 4) enforcement measures and remedies.

More specifically, these proposals call upon VLOPs to complete mandatory risk assessments and technical audit disclosures, offer users an opt-in program for algorithmic curation, disclose the use of AI systems to users, and enable users to request justification about the removal of their content by algorithmic moderation systems used by VLOPs.

To enforce these recommendations, the policy brief outlines the creation of the Canadian Artificial Intelligence Regulatory Authority (CAIRA) to oversee and adjudicate the use of AI systems on VLOPs, implement the technical audit system to assess AI-system reliability and check for discriminatory biases, and prepare and publish publicly accessible technical reports evaluating the compliance of VLOPs with these policies. A further Artificial Intelligence Tribunal will administer monetary penalties on non-compliant VLOPs.

Introduction

Climate Change which manifests itself in floods, draughts, earthquakes and storms, in displacement, migration and deprivation, in a threateningly irreversible destruction of biodiversity, human and non-human livelihood. A global economic and financial system deepens already staggering socio-economic inequality. After decades of shifting public finances, services, and responsibilities to the market, we are facing uncertain prospects for a 'green' reorientation of the global financial system. The context in which transformative political change must be attempted, is marked by radicalization and political polarization. Even after a historically unique global pandemic, in which much of the violent and exploitative infrastructure of global value chains has become more visible than ever before, the call for a 'return to normal' exudes its seductive appeal. As the economic might of 'big tech' increases, so does the sector's political prowess. Democratic deliberation threatens to be diffused, derailed and undermined by the noise, the anger and too many hours spent in the increasingly toxic spaces online.

The current crisis is multidimensional. It is political and, at the same time, challenges every element of the political system. It touches lives, communities, and environments all over the world. No one is an island, and we are all in this together. The climate crisis today challenges prevailing assumptions regarding growth and progress and lays bare the exploitative and destructive dynamics of how the affluent relate to, benefit from, and discriminate against those that are vulnerable.

How can transformative action be organized – and, sustained? What is the role of governments, businesses, civil society actors, and educational institutions? Who should lead, and how can a larger movement be created - and kept alive?

The Academy of Transformative Business Law came together in Montreal in May 2023 to address the multifaceted challenges that confront governments, business, and civil society actors in a context for which the clock has been ticking. The participating Fellows came from eleven countries and brought their interdisciplinary expertise and their diverse experiences into a lively and intensive conversation.

With a focus on how modern businesses continue to be run, their work focused on the promises and the contestable variations in implementing robust corporate governance changes towards an institutional practice geared to ESG, diversity, and inclusivity. The Academy's work explored the multi-tiered and historically entrenched system of financing through debt and equity, locally, nationally, and globally from the perspective of how to achieve a forward-looking regime of sustainable finance. The Academy explored the challenges of understanding and conceptualizing, proceduralising, and implementing what must be a comprehensive, all-transforming enterprise for law, economics, and politics of climate change governance. The organization of global financial and economic exchanges requires the acknowledgement of the key role played by global value chains and their constituting role in organizing and structuring real-world opportunities of access and participation but also of extraction and exploitation. Finally, we need to acknowledge the dramatic reconfiguration of the 'public sphere' under the influence of big tech's expansion and intrusion into every conversation, thought exchange and transaction. Today's challenge for lawyers, business people, public service or union leaders, industrial organizations, policy makers and citizens consists of drawing the connections between the here depicted, seemingly disparate crisis elements. The following five sections of the inaugural Academy's first Impact Paper are meant to help map the problem landscape in which we find ourselves today. Of course, the here presented analysis is by default an only abbreviated one and its authors welcome any feedback and further input.

Chapter I – ESG and the Purpose Economy

A - Introduction

The Problem

Canadian society, like many other countries, is currently struggling to address pressing environmental and social challenges. Mass movements such as Fridays for Future, Black Lives Matter, and #MeToo demonstrate public frustration at the lack of progress on these critical issues. In today's economic system, a huge portion of the world's wealth and power is in the hands of corporations. Harnessing corporate power for social and environmental good, therefore, plays a key role in tackling the challenges humanity faces, especially in meeting global climate targets.

A majority of investors throughout the world have a single goal: to earn the highest financial return.[1] Focusing solely on maximising financial return on investment for the shareholder ignores environmental and social value and perpetuates wealth and racial inequality.[2] For example, 47% of Canadians live paycheck to paycheck[3], and Canada has one of the largest gender wage gaps among industrialised states.[4]

Context

Historically, a major barrier to corporate social purpose adoption has been courts' interpretations of fiduciary duties (the legal duties owed by corporate directors) as the protection of shareholder interests above all else. In 1919, the Michigan Supreme Court declared in *Dodge v. Ford* that directors could not act in interests apart from those of shareholders.[5] The court stated that the primary purpose of a corporation was the profit of the shareholders, and that directors had to pursue that goal.

In Canadian corporate law, there have been major shifts in this regard, especially in recent years. Notably, "courts have confirmed the lawfulness of directors taking into account a wide range of stakeholder concerns in exercising their fiduciary duties, which

are owed to the corporation, not to shareholders."[6] In two key Supreme Court of Canada decisions, the Court has clarified that directors' fiduciary duties require them to act "in pursuit of the realisation of the objects of the corporation," as opposed to the interest of shareholders exclusively.[7] These cases – *People's* and *BCE*, respectively – emphasize that while fiduciary duties of directors in Canada are duties owed to the corporation itself, this shall not just mean shareholders.

The decisions in *Peoples v. Wise* and *BCE Inc. v. 1976 Debentureholders* opened the door to corporate leaders making decisions based on long-term environmental and social factors without breaching fiduciary duties.[8] However, a more transformative approach is needed in order to permit and incentivise companies to act in a socially and environmentally beneficial way. There is a considerable difference between corporate directors having the legal *ability* to slash profit margins for environmental and social reasons and having a *mandate* to do so. **In the absence of a corporate purpose that is related to the public interest, directors who act in the best interests of corporations are still effectively limited to pursuing the purposes of maximisation of profit and share value.**

B - The Purpose-Driven Economy: From Imagination to Solution

In response to this problem, the concept of the purpose-driven economy has emerged. The idea of the purpose economy builds on and engages with decades of academic and policy work around 'CSR' – corporate social responsibility. According to this new approach, a corporate purpose statement is meant to be required for each business filing its registration papers. Such a statement "explains why a company seeks to benefit from corporate status [...] It provides the underpinning to the corporation's operations."[9]

An example of a successful corporation with a public purpose is the Makivik Corporation. The Makivik Corporation's shareholders are the Inuit beneficiaries of the

James Bay and Northern Québec Agreement (JBNQA), and its corporate purpose includes alleviating poverty among Inuit, developing Inuit communities, and fostering Inuit culture.[10]

Corporations that wish to conduct themselves with a social or environmental purpose face barriers that profit-driven corporations do not. If there is to be a fundamental shift towards a purpose-driven economy, more needs to be done to encourage and facilitate this shift at all levels. **This policy memo will outline five concrete recommendations aimed at accelerating the shift towards a purpose-driven economy.**

C - Recommendations

Recommendation 1: Require Corporations to State their Social Purpose

Target Audience: Federal and Provincial Governments

Actions:

a) **Require corporations to state a corporate purpose in their articles of incorporation.**
b) **Encourage corporations to make binding ESG statements in their by-laws.**

Problem

While the state plays an important role in governing corporate behaviour due to its position as the grantor of corporate status, corporations are, in many ways, self-governing entities. Sources of corporate governance include articles of incorporation and by-laws. Canadian law currently does not require corporations to make a statement of purpose within their articles of incorporation or by-laws.[11] In fact, the *Canadian Business Corporations Act (CBCA)* does not currently require corporations to have by-laws.

Obstacles

Jurisdictions compete to attract corporate incorporation based on existing regulatory frameworks.[12] As a result, while corporate law must evolve to meet the challenges that society faces today, it tends to simultaneously strive to remain competitive with other jurisdictions to avoid an exodus of corporations that have the option to incorporate elsewhere, a phenomenon often called "jurisdiction shopping."

Another obstacle to requiring changes in by-laws rather than in, for example, the binding incorporation articles, is the implied reliance on soft law. Since by-laws are not legally mandated, there is at present no obvious mechanism to make the inclusion of social purpose in them mandatory.

Solutions

Any proposed ‘solution’ will be evaluated and assessed against the fact that an overwhelming number of business practices remain far below the standards that have been emerging as a result of an ever more intensifying debate. Complementing decades-worth of policy work within company law, corporate governance and CSR, there is today a wider, more inclusive range of critical attacks on the citadel of a corporate law still largely dominated by principles of shareholder value maximization and liberty of contract. Haudenosaunee law provides an example of a more sustainable, forward-looking lens: the Haudenosaunee “Seven Generations Principle” intervenes in the prevailing short-termism of corporate law and argues that decisions should be made on the basis of how they will impact the world seven generations from now.[13] Drawing on this inspiration, our first policy recommendation cited above aims to encourage corporations to consider and explain in their articles of incorporation and by-laws how their business strategies and corporate practices will affect the world throughout future generations.

Once a critical mass (Coro Strandberg suggests 25%) of corporations have adopted purpose-driven business models, other corporations will follow in a snowball effect.[14] Early adopters of forward-looking business models will pioneer the shift towards

a purpose-driven economy by voluntarily embedding social purpose within their articles of incorporation and by-laws.

Action Item for the Federal Government:

1. **Articles of incorporation:** As stated by Iseoluwa Akintunde (PhD Candidate, McGill Law) and Richard Janda (Associate Professor, McGill Law) in their January 2023 Report for the David Suzuki Foundation, the wording within *CBCA* subsection 122(1.1) of "may", instead of "should", fails to sufficiently incorporate purpose within corporate governance. ***Therefore, amending the CBCA subsection 122(1.1) to "should" ensures that the purpose-driven economy is institutionalised within business practices.***[15]

An example of a legal framework enabling corporate purpose can be found in France. In 2019, France passed the PACTE Act no. 2019-486. Among the effects of this law was the creation of a new Article 1833(2) in the French Civil Code, which requires that corporations be managed in line with their social purpose, taking into account social and environmental factors. The law also allowed companies to set out their "raison d'être" in their by-laws.[16]

Recommendation 2: Reporting for Stakeholder Transparency

Target Audience: Canadian Federal Government: Environment and Climate Change Canada, Health Canada, the Health Products and Food Branch, and the United Nations.

Actions:

a) **Implement a public product rating system, which would rank products on ESG. The government should draw on the NFPA 704 system for identifying chemical substances as an example of how this ranking can be structured [Figure 1].**

b) The United Nations should hold an international conference with key global actors. A worldwide metric system quantifying ESG must be created, using an industry-specific approach.

Reporting for consumer transparency purposes needs to be concise and simplified, since consumers do not tend to do sophisticated research on companies' products or services. Therefore, there is a need for a concise labelling system so that a consumer can quickly and easily assess a company's ESG performance. This can be achieved through the implementation of mandatory ESG labelling of products (for an example, refer to figure 2). The creation of a mandatory ESG labelling on consumer products would create an ecosystem for competition and incentive for companies to progressively seek improvement in their business processes. This public rating will supplement private certification badges, such as B-Corp, Vegan certified, etc. This public ESG labelling could be facilitated through Environment and Climate Change Canada, Health Canada, and the Health Products and Food Branch.

Figure 1

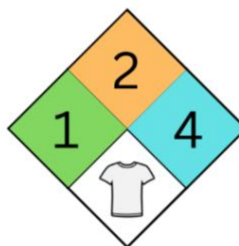


Figure 2

Legend
Green = Environment
Orange = Social
Turquoise = Governance
White = Symbol of industry (Ex: fashion)

<u>Problem</u>

A major problem with ESG is the lack of standardized criteria and reporting requirements for what makes an investment sustainable.[17] Private ESG certifications exist, such as B Corp,[18] but are optional and the distinction between sustainable and non-sustainable products lacks in nuance.

Obstacles

The absence of universal ESG metrics may be delaying governments from implementing a public ranking system. In 2018 Japan's Ministry of Economy, Trade, and Industry created a label identifying companies that report on ESG performance - but progress must go further.[19]

A) Securities Disclosure Obligations

Target Audience: Provincial Governments and Securities Regulators

Actions: Securities regulators must enact a national policy mandating uniform ESG and purpose-related disclosures.

Securities regulators must enact a national policy which mandates uniform ESG and purpose-related disclosures. Under current securities regulation, public corporations have enforceable disclosure obligations.[20] For example, they must release annual financial statements that meet a variety of formal requirements. Further, under National Policy 52-109, a public corporation's Chief Executive Officer (CEO) and Chief Financial Officer (CFO) must sign and certify these disclosures. These mandatory disclosures can be enforced by numerous stakeholders, including securities regulators who are granted broad powers to intervene in the public interest, including cease-trade orders, financial penalties and binding remedial orders.[21]

We propose adding a further disclosure obligation which would need to be related to ESG and corporate purpose. Public corporations would have to disclose several metrics and answer questions related to their company's ESG position, objectives and mechanisms. The content of these disclosure obligations would also have to be certified by the CEO and CFO, like other disclosure obligations, which would engage their personal liability.

Similarly, securities regulators could intervene in the public interest where these disclosures are not sufficient or go awry in any respect.

Problem

There is a persistent lack of enforceable and consistent disclosure obligations. Public corporations are able to make statements with little risk of regulatory sanction, and there are no consistent reporting obligations.

Obstacles

Regulatory burdens on meeting disclosure obligations.

Solutions (2a and 2b)

- **Mandate reporting.** A government-administered ranking system would require that all companies report on ESG - even the big polluters. Increased transparency will have a meaningful impact for three key audiences: financial institutions, investors, and consumers. Implementation of these recommendations would assist these three target audiences in making a well-informed decision. This spectrum promotes ESG competition between companies while averting purpose-washing.
- **Creating ESG metrics enables us to consider factors beyond financial metrics.** The profit-driven economic structure is rooted in a misalignment of values, which prioritises economic profits while disregarding or miscalculating the true and much wider cost of business. Universal ESG metrics enable businesses to measure environmental and social costs.
- **Give transparency to consumers.** Diagrams allow consumers to easily discover the ESG performance of corporations. This empowers consumers to act on ESG information.
- **Spotlight high-impact sectors like oil and gas, garment, in particular fast-fashion, food, transport, chemicals, and construction.** The disproportionately negative

environmental and social impact of a small number of businesses in the energy, agriculture and food, transport, construction, chemicals and garment, especially fast-fashion, sectors[22] must be disclosed with those ESG and corporate purpose reporting obligations.

- **Forcing public companies to disclose ESG and purpose related information in securities disclosures will build transparency and accountability.** These statements will constitute full and plain disclosure and cannot be misleading. This will address purpose-washing since corporate and CEO/CFO personal liability will be engaged.

Recommendation 3: Targeted investment by Public and Private Actors

Target Audience: Federal/Provincial/Local Governments, the Business Development Bank of Canada, Investors, Banks, and Asset Managers

Action: **Encourage the growth of social purpose corporations through increased targeted investment in the public and private sectors.**

<u>Problem</u>

Many social purpose enterprises are initially less profitable compared to solely for-profit businesses. As a result, social purpose enterprises face difficulty accessing traditional financing.[23] Purpose-driven firms may generate less profit but may instead generate social and environmental returns. This results in a "financial-social return gap."[24] This term highlights the risk that social enterprises will be chronically underfunded relative to the benefits they create.[25]

<u>Obstacles</u>

Investors, asset managers, and banks generally prioritise financial return on investment. There is a systemic undervaluing of social and environmental return on

investment. As a result, social enterprises are chronically underfunded by the private sector. Meanwhile, public sector investments in social enterprises remain limited.

Solutions

The proposed action items will increase the amount of financial capital that is available to social purpose corporations, thereby eliminating the "financial-social return gap"[26] and helping more corporations to adopt a social purpose as their primary reason for existing.

Action Items for Public and Private Actors

The public and private sectors should increase targeted investment opportunities for social-purpose corporations. The public sector, in particular, may see significant returns from investing in social purpose organisations, since these organisations may achieve social and environmental outcomes that the state would otherwise have funded through public programs.

Specifically, the public sector should:

a) Expand targeted **public investment in social purpose organisations**
   i) The Business Development Bank of Canada should create a new stream of favourable financing that is exclusively available to corporations that have adopted a social purpose in their Articles of Incorporation and perform well on ESG metrics.
   ii) The Government of Canada should scale up the social finance fund,[27] which provides flexible financing opportunities to social purpose organisations.

b) Restrict government **contracting and procurement** opportunities to corporations that perform well on social and environmental *key performance indicators* (KPIs).
   i) The public sector exists to represent the interests of Canadians and manages taxpayer money. Therefore, it should avoid contracting corporations that perform badly on social and environmental KPIs.

ii) In requests for proposals and calls for submissions, the Government of Canada should seek not only the contractor that proposes the lowest cost but should score contractors based on environmental and social KPIs.

In the private sector:

a) **Asset managers** should ensure that investment portfolios that are labelled as "ESG" only contain stocks in corporations that have a social corporate purpose and perform well on environmental and social KPIs. Asset managers should also recognize that investors have a greater range of interests than profit. Asset managers should inquire about investor priorities and respect the desire of investors who wish to prioritise social purpose investing and seek social outcomes, in addition, to return on investment.
b) **Banks** should consider ESG key performance indicators in determining eligibility for financing. Banks should also recognize the increased long-term risks associated with investing in corporations that perform poorly on social and environmental KPIs. Banks should reduce investment in these corporations while increasing their interest rates.
c) **Investors** should assert their power to request social and environmental return on investment, not only financial return on investment. Investors should also demand greater transparency from asset managers and from corporations so that they can effectively assess the environmental and social return on their investments and assert their right to seek remedies if commitments are not met.

Recommendation 4: Supporting ESG and purpose-driven corporations through taxation
Targeting: Federal Government

Action: Amend the Canadian Income Tax Act[28] to develop a special tax status targeted at organisations that meet ESG-related standards throughout their business practices. This special tax status should introduce (1) a sliding scale corporate tax break targeted

at SMEs and (2) tax incentives to support corporations implementing ESG-conscious business practices.

Problem

Despite the recent federal Clean Investment Tax Credit in Budget 2023,[29] governments, such as the Canadian Government, can further leverage taxation schemes to incentivize businesses to invest in a purpose-based economy. The Brookings Institution argues that tax incentives "can power more equitable, inclusive growth".[30] Targeted corporate tax breaks can be introduced as a financial motivator to encourage corporations to better incorporate sustainable practices within their business models.

Obstacles

Experts from progressive think tanks, such as the Canadian Centre for Policy Alternatives, commonly criticize corporate tax breaks as ineffective and for negatively impacting the state's ability to fund social programming and infrastructure.[31] However, in this case, a targeted, sliding-scale approach allows the state to identify specific categories of business activity while excluding less sustainable business practices.

A targeted, sliding-scale approach to corporate tax breaks, including a maximum, ensures that the initiatives support SMEs to build and grow purpose-driven business practices without disregarding the importance of public funds. Further, using tax incentives to encourage corporations to transition to more purpose-driven business practices will produce long-term benefits for the entire market, creating a snowball effect.[32]

Solutions

The targeted focus on ESG and purpose-driven business through taxation will support SMEs in adopting more sustainable business models. As it relates to larger

corporations, targeted changes will supplement the previous recommendations through tax incentives to support investments in ESG/purpose-driven business changes.

Action items for the federal government:

1. **Special tax status:** The tax system can support the shift to a purpose-driven economy by lowering the tax rates applicable to corporations that meet purpose and ESG criteria. The special tax status would function much like the registered charity status. For example, the Government would develop a status that corporations, such as B-Corporations, could apply for in recognition of their purpose and ESG-oriented objectives and mission. Creating a new special tax status focused on ESGs and purpose-driven businesses will reinforce the Government's commitment to sustainability and equity.

   After receiving this status and registration, companies would be eligible for a tax reduction of 2% on their first $1MM (double the maximum identified through the small business deduction) of active business income and 1% on their next $4MM of active business income. Because operating a purpose-driven company can mean greater input and operational costs, these tax incentives would help alleviate this cost disadvantage, especially for businesses in the early stages of their lifetime. This would mean that such corporations pay a total effective tax rate of 7% on their first $500k of income, 13% on their income between $500-$1MM and 14% on any income from $1MM-$4MM, and 15% on any income above $4MM.

2. **Targeted tax incentives:** The tax system can support the shift to a purpose-driven economy with specific measures to incentivise existing companies to adopt a purpose-oriented approach. This transition can come with costs, such as B-corp certifications, that may be a barrier to transition. The tax system could help alleviate these transition costs by offering favourable tax treatment to transition-

related costs. For example, the cost of B-corp certification and professional fees to amend by-laws could be double or even triple deductible against income.

Recommendation 5: Integrating Social Purpose within Education and Professional Training

Target Audience: Higher education institutions first, followed by industry/trade associations

Action: Higher-level institutions, starting with business and law schools, should teach current and former students about a purpose-driven economy.

Problem

Many higher education institutions offer specific courses or even departments dedicated to sustainability, but such programmes risk forming echo chambers. For social purpose to find roots within our economic system, it is necessary that it be integrated into business, law, and economics curricula.

Obstacles

Galdón et al. argue that the following impediments have slowed down business schools from being leaders in welcoming ideas related to sustainability:[33]

a) **Politicisation**: ESG issues such as climate change, DEI, and inequality continue to spark polarised debates in society. This makes it harder for professional schools to tackle issues head-on, and at the same time stay away from taking partisan viewpoints.
b) **Under-Qualification:** academics in management feel underqualified to teach these issues since climate change is outside of the area of expertise typically tackled by business schools.

Coro Strandberg proposes a solution that she calls "total product recall": bring professionals back to their professional schools for training on purpose-driven economic values. Harvard Business School, for instance, offers a three-week "Sustainable Business Strategy" course about advantageously integrating purpose-driven leadership into management.[34] Intensive programmes like these are valuable, but insufficient on their own.

It is important to go to the root of academic curricula, programmes, such as business, engineering, and law, which should incorporate purpose-driven models throughout their teaching. From courses in business associations, ethics, corporate law, macroeconomics, business strategy, etc., social purpose should permeate core classes in business and law schools, not just electives. This way, social purpose will be built within the structure of students' understanding of their professions.

Solution

By implementing change in academic curricula as well as by re-training professionals in business, law, and other relevant fields, higher education institutions can be a leader in the transition towards a purpose-driven economy. In addition, the recommendations of this Impact Paper offer an opportunity for business and law schools to research and develop the most effective indices for measuring social purpose and ESG impact. This initiative must be further applied to professional and industry trade associations, such as the Business Council of Canada, Chartered Professional Accountants of Canada, and the Canadian Bankers Association, as well as to the provincial equivalents of all such groups and to municipal and regional chambers of commerce.

Chapter I Conclusion

Human society is at a crossroads economically, socially, and environmentally. The

current corporate model focused on profit-maximisation fails to address the true cost of current and long-term business impacts. In contrast, as discussed in this chapter, a purpose-driven corporate strategy promotes ESG and sustainability goals while sparking economic development. The shift from a profit-maximisation model to a purpose-driven model will require a holistic approach. Jurisdictions will promote ESG goals and sustainability by integrating and institutionalising a purpose-driven economic model within government regulations, private/public investments, and corporate culture (Recommendations 1-5). Therefore, in order to act innovatively yet responsibly, this Chapter highlighted a framework to adopt a purpose-driven model to give corporations a leading edge and safeguard citizens' long-term well-being.

Chapter II – Sustainable Finance

A - Introduction

This section of our Report focuses on 'sustainable finance' (SF) not only as a field of immensely rich and diverse activity but also as an enormously ambitious normative proposal. At the core of this proposal is the assumption that it will or should be possible that financial markets may be able to effectively mitigate or prevent climate change. A closer investigation into this ambitious claim reveals a number of challenges – these include the difficulty in *identifying the most suitable actors* who should be in charge of assuming roles of agency, intervention, and more. Other challenges include the *identification of and the choice among different policy options*. Yet another difficulty concerns what we call 'implementation challenges,' in other words, the question of whether a) private actors must be forced to act or b) they will act on their own.

In an effort to map SF's constituency, we have identified both public, governmental actors and private actors, namely financial and non-financial institutions. As we present our

findings and recommendations in focusing largely on Canada, we are proposing the use of an imaginary, yet desirable institutional addressee, whom we refer to as the "*Ministry of Sustainable Futures*." The MSF is not meant to displace existing authorities on the federal or provincial levels but to invite reflection on the design of a democratic agency that may act with insight, information, courage and ambition in working together with private business and civil society actors to bring about robust foundations for sustainable transformation. The following sections illuminate the particular positions held by these actors in this contested policy field.

B - Support Institutional Investors In Building Green Portfolios

Background: The Barriers to Transitioning to a Sustainable Portfolio

In Canada and worldwide, institutional investors have a legal duty to make investment decisions in the best financial interest of their beneficiaries. However, there is a spectrum of viewpoints on whether or not these fiduciary duties limit institutional investors from aligning their investments with climate compliance objectives. It is further debated whether if they have the potential to facilitate the adoption of prudent yet ambitious measures to achieve domestic and international targets for reducing greenhouse gas (GHG) emissions. The increased pressure of disclosure for 'dirty assets' creates a further incentive for greening the portfolio, while emphasizing the importance of considering the long-term implications of climate change on asset prices[35][36].

Nevertheless, the financial sector's historical dismissal of sustainability's value and the quest for profit maximisation pose substantive obstacles to transitioning to a green economy. Divesting from carbon-intensive industries and investing in green projects often conflicts with investors' fiduciary duty that traditionally prioritizes shareholder interests over green investment because those can be scrutinised as breach of duties due to being less profitable.

Therefore, there must be a shift from shareholder primacy to stakeholder primacy that considers a broader range of actors' needs and concerns[37]. Under stakeholder primacy, institutional investors are encouraged to consider the environmental impacts of their practices, as planetary boundaries and climate change pose limitations to long-term profitability without proper adaptation[38] and emerging literature challenging the notion that green investments are less profitable[39]. Climate-related risks, including physical risks, liability risks, and transition risks, affect issuers and institutional investors, reinforcing the need for environmental consideration[40]. Additionally, the *Canada Business Corporations Act* (CBCA) allows directors and officers to consider the interests of multiple stakeholders, including ESG factors, when making investment decisions in green projects[41].

While divestment campaigns and decisions are important, they do not directly impact the access to capital of carbon-intensive issuers. To support the green transition, sustainable policies should assist in phasing out polluting industries rather than solely dropping "brown" shares. However, divestment decisions by large institutional investors can send signals to the capital markets about the unsustainability of carbon-intensive assets and influence other financial actors.

It is important to acknowledge that divestment is just one tool available to institutional investors for achieving climate compliance and may not always be the most effective option. Other tools to promote climate compliance include the engagement with management through direct communication, proxy voting campaigns, and stakeholder litigation. The choice among these approaches depends on how the institutional investor assesses their fiduciary duties and on the specific circumstances. In general, divestment is likely to be more suitable for challenging assets like carbon majors and potentially less appropriate for sectors such as real estate and transportation.

Recommendation I

(A): ***Institutional investors should be given maximum flexibility, incentive, and protection in making investment decisions that are climate-compliant and that contribute to meeting the Canadian domestic and international obligations to reduce GHG emissions.***

(B): ***Institutional investors should be required by financial regulators to disclose the climate risks in their portfolios at the asset and portfolio levels.***

(C): ***The federal government should encourage investment in green technologies and economies by providing appropriate tax incentives.***

Institutional investors should be provided protection in making decisions to transition to a sustainable portfolio through legislative "safe harbour" rules, such as: amending the standard of care that applies to institutional investors to clarify that divestment from carbon-intensive assets is not a breach of fiduciary duty, and through legislative ordinance that limits causes of action against institutional investors who decide to divest from carbon-intensive assets.

As directors of institutional investors consider divestment from carbon-intensive industries, they may face potential legal and financial risks, including lawsuits from stakeholders who disagree with these decisions. Providing legal protection to fund managers against potential lawsuits arising from divestment decisions helps reduce the legal risks of being sued by the shareholders due to the breach of fiduciary duties[42]. This protection gives institutional investors the confidence to divest and align their portfolios with sustainable investments. Historically, institutional investors were pressured to withdraw their investment from South Africa following boycotts of their stocks[43].

In order to provide an incentive to transition to a sustainable portfolio, institutional investors should also be required to disclose the climate risks in their portfolios to their

beneficiaries and to regulators. Disclosing climate risks in a portfolio should include disclosure on an individual asset basis, as well as on a portfolio as a whole basis.

i. **Disclosure:** All institutional investors should publish reports on their decarbonization efforts that clearly list their holdings and include their transition plans in alignment with climate commitments. Disclosure on a portfolio basis allows beneficiaries and regulators to assess an institutional investors' progress toward a sustainable portfolio, and to hold institutional investors to account in the management of their assets. Disclosure of individual investments' climate risks will incentivize potential investees to properly measure and disclose their climate risks (and climate-compliance strategies).
ii. **Divesting and Tilting:** Institutional investors should prioritize divestment from carbon-intensive projects, such as fossil fuels, and reallocate those resources towards green projects. Where appropriate, asset managers could be encouraged to adopt a 'tilting' strategy, whereby the investor 'tilts' away from 'brown' industries while holding shares in selected lead-firms that can take action to lower their carbon footprint (e.g., an oil and gas company developing clean energy) and thereby attract other firms to follow[44].

Publishing reports on decarbonization efforts and transition plans can create a framework for transparency. The specific details of reports and plans should be tailored to the unique circumstances of each investor, taking into account their overall investing style and the investment time frame. For instance, direct conversations with executive management or collaboration with other institutional investors can be viable approaches, in line with proxy voting guidelines. Most importantly, this transparency helps investors fulfill their fiduciary duty by providing them with accurate information about their decarbonization initiatives. By providing accurate and comprehensive information about their decarbonization initiatives, institutional investors fulfill their fiduciary duty and enable more informed decision-making that prioritizes the long-term interests of all stakeholders.

Establishing robust disclosure requirements for public pensions funds can also mitigate litigation risk. While there are currently no pending cases against Canadian pension funds, beneficiaries other jurisdictions like Australia and UK have brought lawsuits against trustees alleging a failure to identify and disclose climate risks[45]. On the other end of the political spectrum, plaintiffs in the United States, represented by Donald Trump's former Labor Secretary Eugene Scalia, are currently suing three New York City pension funds for a breach of fiduciary duties due to sales of fossil fuel assets worth approximately US$4 billion[46] (Wayne Wong v. NYCERS, TRS and BERS, New York State Supreme Court, New York County).

The federal government should protect divestment decisions that cause losses and promote investments in green projects by providing appropriate tax incentives. These could include tax credits, deductions, or exemptions to institutional investors who are transitioning their portfolios. Offering tax incentives, such as tax credits, for losses incurred in the early stages of investing in green projects can help limit the financial risk associated with these investments. Through tax incentives, institutional investors may be eligible to claim tax credits for losses incurred due to investing in green projects. Tax incentives can be used to encourage investments in environmentally friendly initiatives, renewable energy and clean energy projects. These incentives can take the form of tax credits, deductions, or exemptions, and can be designed to offset the financial risks associated with early-stage investments in green projects. By reducing the financial burden, more investors may be encouraged to support green projects, driving the transition towards a sustainable economy.

C - Canada Should Catalyze Flows of Capital and Technology to Developing Countries for Climate Mitigation and Adaptation and Monitor and Assess these Flows.

Background: Canada has committed to increase the flow of climate finance and technology to developing countries

Low and middle-income countries are disproportionately affected by climate change, and the most unlikely to transition towards sustainable and low-carbon economies, owing to a lack of capital and technology. The Paris Agreement entrusts developed nations with the responsibility to mobilize financial and technical resources to assist developing countries in meeting their climate change obligations[47].

Current flows of capital and technology to developing countries for mitigation and adaptation are insufficient. Developing countries have limited access to climate technologies that reduce GHGs[48] [49]. Hence, finance mobilization is crucial in allowing developing countries to access to capital and climate technologies, particularly regarding the role of private resources in funding adaptation measures[50]. Developed countries can do more to enhance mechanisms for channeling private resources in low-income countries. Until now, private climate finance has targeted middle-income where projects usually are considered low-risk profiles. Between 2016 and 2020, Least Developed Countries received just 17 percent of total climate finance, while low-income Countries received 8 percent. Lower-middle-income countries received 43 per cent[51].

At COP 15, Canada joined developed countries in committing to mobilize USD $100 billion/year between 2020 and 2025 to finance climate change mitigation and adaptation in developing countries[52]. This collective commitment, however, remains unfulfilled.[53] To reverse this trend, Canada should mobilize new, more flexible, resources for climate finance and expand access to low-carbon technology, using its domestic institutions and international networks to advance an ambitious, global climate agenda. Canada deploys capital in support of mitigation and adaptation in developing countries through 1) Domestic agencies–notably Canada's development finance institution, FinDev Canada; and 2) Multilateral Development Banks (MDBs) of which Canada is a member. In addition, Canadian climate technology has the potential to mitigate emissions and build resilience if deployed in developing countries. Canada's approach to all three aspects can be improved.

Recommendation 2

> **(A):** ***Canada should strengthen its Development Finance Institution to catalyze low-carbon growth in the poorest countries.***
> **(B):** ***Canada should mobilize Multilateral Development Banks to be more ambitious, risk-tolerant and flexible in providing climate finance to developing countries.***
> **(C):** ***Canada should bring together its business and trade promotion organizations behind a comprehensive plan to deploy made-in-Canada climate solutions in developing countries.***

Canada was the last G7 country to create a development finance institution. Initiated in 2018, FinDev Canada has climate change among its top priorities. While FinDev Canada has financed investments in agribusiness, renewable power and various blended financing mechanisms in Sub-Saharan Africa, Latin America and the Caribbean, its budget–$300 million over five years–is low compared to Canada's OECD peers. For instance, the Dutch DFI has a committed portfolio of over €12 billion, while the UK's British International Investment's portfolio exceeds $7 billion. The German, French, Spanish and Norwegian DFIs, too, are all significantly larger than Canada's[54].

To move developed economies toward the $100 billion target, **the Government of Canada should triple its climate finance commitment from $5.3 billion over five years[55] (2021-26) to over $3 billion annually.** This would place Canada's contribution toward the Copenhagen target in line with Canada's share of total GDP of OECD countries (3.7 percent in 2021).

Beyond its own institutions, Canada must leverage its privileged position to advance an ambitious global climate finance agenda. As a G7 and G20 member, and shareholder in all major multilateral development banks, Canada has been at the center of efforts to renew and reshape the work of MDBs in light of climate change. Canada has established climate-focused blended finance programs worth over $800 million with the IFC, AfDB, IDB and ADB, and remains a trusted partner in strengthening the institutions of the rules-

based international order[56]. Therefore, Canada must push multilateral development banks to do more on climate.

In anticipation of climate shocks over the next decade, however, these institutions must adapt to remain relevant. Canada should be ambitious in driving change. This change must address the following:

i. **MDBs must increase their risk appetite to help ignite low-carbon growth in the poorest countries.** The IFC, which maintains a $60 billion portfolio, zealously guards its triple-A credit rating, which requires it to sustain levels of risk, capital adequacy and liquidity that ensure an almost zero risk of default on their financial obligations. This reluctance to embrace greater risk lessens the flow of finance to the least developed countries. IFC's net investment in low-income countries (i.e., International Development Association borrowers) fell from $2.1 billion in 2011 to 1.7 billion in 201[57].

ii. **MDBs must offer more flexible financial instruments.** Leveraging their regional presence, MDBs should play a leading role 'upstream' in putting climate deals together, working with the private sector and local stakeholders to facilitate commercial private finance. This will entail the co-creation of investment opportunities, tackling impediments in the investment climate, development of investment pipelines, supporting local market development, effective risk mitigation instruments deployed at scale, and blended finance to reduce cost of capital.

iii. Canada could **make an anchor contribution of capital to a new financing window at the World Bank to deal with climate** and other global public goods[58]. This would support countries like Brazil or Indonesia, for example, to take more action on deforestation by offering access to World Bank financing at lower-than-normal interest rates that take into account the benefits of these programs to the rest of the world. Canada could mobilize its G7 and G20 partners, and major philanthropies (Gates Foundation, Bezos Fund, the Nature Conservancy).

iv. **Canada should be creative in identifying other opportunities to exercise climate leadership at MDBs**. In May 2023, for example, Denmark, Japan, Korea, Sweden, the UK and US agreed to provide $3 billion of guarantees for the Asian Development Bank's portfolio that will mobilize $15 billion in additional climate lending. Canada could replicate this model at the other MDBs to unlock additional dollars at low cost to donors.[59]

Ultimately, the need to create an enabling environment for faster scaling and diffusion of climate technology in developing nations must be addressed. Exporting technology solutions to developing nations can help open pathways to decarbonized growth and development. In addition to enhancing access to vital alternative low-carbon products built by Canadian businesses, these businesses can themselves benefit from demand in new markets. Canada should therefore adjust its programs to serve its foreign policy goals by helping innovative, green Canadian businesses to enter new markets in the global south. For example, Canada could mandate and resource Export Development Canada (EDC), the Business Development Bank of Canada, the Canadian Commercial Corporation and Trade Commissioner Service to deliver a consolidated strategy that deploys more made-in-Canada climate solutions in the developing world.

D - Develop Uniform ESG Reporting Standards And Provide Support To Companies In Compliance

Background: Non-uniform ESG Measurement and Disclosure Standards Hinder Investment Decision-making and Assessment

The absence of unified environmental, social, and governance (ESG) reporting standards in Canada is blocking progress in sustainable finance and requires immediate attention. Despite the adoption of mandatory climate-related disclosures in leading financial hubs such as the U.K. and Germany, Canada lags behind in implementing comprehensive reporting standards[60].

This gap in ESG reporting standards undermines Canada's commitment to sustainability. It hinders the growth of responsible investing as well as the allocation of capital towards environmentally and socially beneficial projects and investments. Without clear and consistent ESG standards, investors face challenges in accurately assessing the sustainability performance of Canadian companies and projects.

Moreover, in the absence of a robust regulatory framework, corporations are not incentivized to adopt sustainable business practices, which impedes progress towards a greener and more equitable future. To address this problem, it is imperative for Canadian authorities, financial institutions, and other stakeholders to collaborate in order to establish a clear set of ESG standards that promote transparency and accountability, and that align with global best practices. Only through such concerted efforts can Canada unlock the full potential of sustainable finance and contribute meaningfully to the urgent global sustainability agenda. Corporate ESG disclosures across companies cannot be compared since they are not based on common metrics[61].

There is also a lack of training and knowledge regarding ESG reporting in both the public and private sectors. The primary difficulties of standardizing ESG reporting include: company-specific nature of ESG issues; obtaining accurate and easy-to-understand ESG information; involvement of non-quantifiable ESG information; and subjective ESG metrics[62]. Without reliable company ratings, investors and governments are hampered in their ability to make business decisions regarding new projects, financing, and investments.

There is an intense debate over whether or not regulators should heighten ESG reporting requirements. On the one hand, there is a rising call for disclosing more material climate risk. A broad range of stakeholders agree that Canadian companies should enhance climate-related financial disclosures. Those include the federal government, the Ontario Securities Commission ('OSC'), the CEOs of the eight largest Canadian pension plan investment managers, the 10 largest pension plans in Canada, and the Canadian Bond

Investors Association ('CBIA')[63]. In particular, 61% of the CEOs in Canada admitted that they were facing growing demand from stakeholders for upgrading ESG reporting and transparency[64].

On the other hand, there remains considerable criticism in the industry about the growth of ESG and tightening ESG reporting regulation. For example, the Canadian Association of Petroleum Producers ('CAPP') points out that mandatory climate-related disclosure may increase the regulatory burden and result in additional costs to the companies operating in the oil industry[65]. Moreover, PwC's latest report suggests that generally Canadian companies are not yet prepared for mandatory ESG reporting[66]. A majority of companies are not certain about what type of information they should include in the ESG reports and how to collect credible information[67]. Besides, 20% of the CEOs in Canada stated that they did not have a sufficient budget to invest in ESG transformation[68]. Shareholders of some leading banks in Canada are asking banks to slow down in their support of climate goals and to maintain support for the oil and gas sector[69]. These dividing lines are bound to grow deeper as some Canadian banks are still heavily financing fossil-fuel companies[70] in a climate that appears to be moving towards more and more robust ESG reporting regulation. In that vein, the European Supervisory Authorities (EBA, EIOPA and ESMA) published their progress report on 1 June 2023, in which they put forward a "a common high-level understanding of greenwashing applicable to market participants across their respective remits – financial markets, banking, and insurance and pensions."[71] This pronouncement was driven by the realization that greenwashing, i.e. "a practice where sustainability-related statements, declarations, actions, or communications do not clearly and fairly reflect the underlying sustainability profile of an entity, a financial product, or financial services (…) may be misleading to consumers, investors, or other market participants."

In the context of diverging, non-uniform ESG reporting standards and surging occurrences of 'greenwashing', Environment and Climate Change Canada (ECCC), the

department within the Federal government of Canada, needs to take the lead and release official definitions of key terms such as 'ESG', 'Sustainable Finance' etc. in order to minimize ambiguities and confusion related to ESG reporting and company ratings. Specific to institutional investors, investment funds should be required to incorporate ESG factors and climate issues into their risk assessment management system, disclose how they have incorporated ESG factors into their investment strategies, and make regular reports to the securities authorities.

In a 2021 report, the Standards Council of Canada noted that the failure to adapt existing approaches to building and renewing Canada's infrastructure is likely to result in 300billion dollars in additional costs. The Council's report highlighted that "over a third of municipal infrastructure needs to be fixed or replaced. This is where standards come in. Canada needs infrastructure standards that reflect the climate of the future, not the past."[72]

Echoing this view, the First Annual Report by the Net-Zero Advisory Board to the Canadian Minister of Environment and Climate Change, issued in January 2023, starts its list of recommendations with a demand for formalization and standardization:

> "*The Government of Canada should direct that all federal agencies, departments and Crown corporations publicly articulate their role in helping Canada achieve net-zero emissions. The Government of Canada should then empower these organizations to play a more ambitious role by formalizing net-zero objectives in their corporate mandates, changing mandates if required, ensuring that executive compensation is meaningfully and transparently linked to climate mitigation performance, and applying common reporting standards.*"

Introducing mandatory ESG reporting in Canada will benefit from reference to international standards and best practices while building on already ongoing national efforts to develop more uniform reporting standards, including for gender and diversity reporting. With the Canadian Securities Administrators (CSA) stepping into the shoes of an absent, federally authorized, Canadian securities regulator to liaise between the different local regulators, there has been a notable tightening of reporting requirements

nevertheless. In a January 2023 report on ESG laws in Canada, published by the *International and Comparative Legal Guides* (ICLG), the CSA's activities in the area of corporate governance have been lauded as both constructive and sensitive to the insight that, "many corporate governance matters cannot be prescribed in a 'one size fits all' manner."[73] Regarding "disclosure requirements regarding climate-related matters for reporting issuers (other than investment funds), securities regulators have been turning the screw towards the inclusion of "governance-related climate disclosure to be included in a reporting issuer's management information circular." Meanwhile, the International Financial Reporting Standards (IFRS) Foundation, in October 2021, the International Sustainability Standards Board (ISSB) launched a consultation process to formulate global sustainability-related disclosure standards which are widely noted to go beyond those of the CSA.[74] Both the CSA and SEC have expressed interest and support for the ISSB[75].

Recommendation 3

> **(A):** ***The federal financial regulator (Office of the Superintendent of Financial Institutions) and the Department of Finance should develop uniform, benchmark ESG reporting standards for each sector and for each asset class to enhance accountability by creating an objective rating standard to assess the environmental risks of each company.***
>
> **(B):** ***The federal and provincial governments should provide financial, training and technical support to small and medium size businesses who may face difficulties in reporting on ESG issues.***

Within the Canadian context, the standardization of ESG reporting needs to be encouraged across each province and region in a way that takes into account the unique challenges each region faces so that standards are uniform. Similarly, particular sectors that have urgent ESG reporting issues (i.e. Oil & Gas, non-renewable energy projects, building retrofits etc.) should be prioritized. Collaboration between public and private

sectors is recommended so that the ongoing concerns of all key stakeholders are given a voice, and so ESG reporting requirements are adjusted according to stakeholder feedback.

In a similar vein, companies need to be encouraged to engage third party verification of ESG reporting so as to improve the credibility of their reports. Investment funds should be required to disclose how they have incorporated ESG factors into their investment strategies so as to raise transparency. ESG factors and climate issues should become part of an investor's risk assessment management system, and they should be required to make regular reports to the provincial securities authority so that a nationwide climate risk assessment mechanism can be developed and applied more broadly.

Funding should be earmarked to provide additional training and support to the companies that lack skills and techniques to report on ESG issues. In addition to specific regional and sectoral challenges, attention should be directed at small and medium-sized enterprises (SMEs) that lack resources to comply with new ESG reporting requirements. This could include a simplified reporting process for SMEs, as well as digital platforms that are user-friendly and serve as a hub for the exchange of best practices and resources.

E - Enhance Supervision of ESG Rating Agencies

Background: Divergent ESG ratings offered by different ESG rating agencies hinder the growth of sustainable finance

In assessing companies' ESG performance, investors and the other stakeholders usually refer to the ESG ratings offered by professional firms, such as S&P, Refinitiv, MSCI, and Sustainalytics[76]. Nonetheless, ESG ratings submitted by different agencies may vary considerably, hence investors need to understand the rating methodologies adopted by various agencies[77]. Although ESG ratings play a crucial role in sustainable finance, currently there are no guidelines stipulating the basic criteria for assigning ESG scores to

companies. In view of this, we suggest enhancing the supervision of ESG rating agencies primarily in two aspects.

Recommendation 4

> **(A):** ***Financial regulators should require rating agencies to fully disclose the methodologies adopted to evaluate corporate ESG performance. They should furthermore explain any revisions they have made to previously assigned ESG ratings.***
>
> **(B):** ***Regulators should set up an independent team/body to oversee the work of ESG rating agencies, investigate whether they have complied with the disclosure requirements., and set up an independent team/body to oversee the work of ESG rating agencies.***

Owing to the variances in methodological design and types of data taken into consideration, ESG scores assigned by different rating companies may vary significantly. Sustainable finance can hardly develop in the absence of reliable ESG ratings, therefore it is necessary to upgrade data quality and transparency of ESG ratings[78].

Besides, the credibility of ESG ratings provided by professional firms is subject to severe challenges. Extant research finds that a leading ESG rating agency has made substantial retroactive revisions to the ESG ratings it assigned to some companies earlier[79]. Such practice undermines the validity of ESG ratings, potentially resulting in losses to investors who have relied on those ratings in making investment decisions.

Our proposal can put the work of ESG rating agencies under supervisory oversight, improving the reliability of ESG ratings submitted by professional firms. Given more comprehensive disclosures about the methodologies applied by different rating agencies, investors can understand why there are differences in ESG ratings among different rating agencies and make informed investment decisions.

Furthermore, as rating agencies are required to disclose and justify any amendments made to earlier ESG scores, users can adjust their investment plans in a timely manner. Establishing an independent team/body to supervise ESG rating agencies can avoid potential conflict of interests between regulators and rating agencies, ensuring that regulatory duties are carried out effectively and impartially.

F - Establishing Climate Champions In Key Financial Institutions

Background: Creating the Function of Sustainability in Key Institutions Provides Leadership and Accountability in Transitioning Portfolios and in Financial System Generally

Currently, the elaboration of a taxonomy for green investments, which establishes the categories and measuring metrics with which a lender assesses the sustainability scores of a potential borrower, is left to market self-regulation. In Canada, at present, banks will either take the initiative to focus on promising and robust green projects or continue to work with 'dirty' borrowers.

Considering the widely diverse climatic as well as political landscape across Canada's ten provinces and three territories, this results in highly uneven lending practices. These, in turn, impact the differential speed at which lending for land development, infrastructure and real estate financing (among other lending) will or will not be integrated into a broader, actively pursued transition towards a more sustainable lending practice.

Recommendation 5

> **(A):** ***Require establishment of "Chief Sustainability Officers" in Canadian chartered banks to create, implement and report on each bank's sustainability strategy to the federal financial regulator (OSFI).***
>
> **(B):** ***Require establishment of CSOs in shadow-bank institutions and coordinate with provincial jurisdictions to do the same.***

(C): ***Pass the Climate-Aligned Finance Act to ensure climate considerations are built into federal government financing and operational activities.***

Each of the six Canadian chartered banks should be required to establish the position of "*Chief Sustainability Officer*". The CSO will be responsible for establishing, implementing and reporting the bank's sustainability strategy, whose climate compliance objectives should be equal or better than the Canadian federal government's international obligations (i.e., portfolio is net zero by 2050). The CSO will report each bank's progress toward its targets to the Office of the Superintendent of Financial Institutions regularly. OSFI should also develop similar requirements for shadow-bank lenders and major institutional investors in Canada. The federal government should also pass the Climate Aligned Finance Act[80].

A CSO would not only be the coordinating and steering agency within a financial institution to elaborate and apply the taxonomy to guide its medium and long-term lending practices, say with time horizons of 2030, 2040 or 2050. It would also be a key nodal point in the knowledge generation department of the institution, responsible for the coordination of data collection, processing and interpretation towards the bank's development and implementation of a comprehensive sustainability strategy.

The CSO would be in a position to effectively address the prevailing divergence and synergy loss across fragmented assessment, certification and lending practices. There is a further significant transformative element inherent to the creation of an Office of Sustainability internal to the financial institution. This differentiation of the institution's governance infrastructure feeds back into the evolving system of professional education in commerce, business and law programs. The creation of the CSO would loop back into the design of appropriate and practice-informed curricular streams geared towards an ESG-based financial sector.

This 'looping' can be achieved by drawing on standing experiences within environmental and climate change governance as well as within specialized human rights programs. As Amanda Machin of the University of Agder in Norway notes, "there are valuable climate imaginaries found in the Global South and by Indigenous peoples that are often overlooked."[81] In these fields, it was the focus on how to amplify and empower neglected interests and alternative, including Indigenous knowledges[82], which drove the implementation of ombudsperson offices.[83] As benchmarks of institutional innovation, these offices are marked by their focus on improving governing processes that reduce litigation events. In alignment with an expanding move towards a more diversified stakeholder-knowledge integration, the CSO would represent the launch of an interactive, dialogical process to generate better and more applied data in distinct sectors and industries.

G - Providing Democratic Climate Leadership in Finance and Development of the Green Energy Sector

Background: Leadership and Ability to Absorb Financial Risk in a Public Entity

Recommendations 1-6 above all address the incentives necessary to facilitate private financial allocation toward a green economy, including (but not limited to) energy production innovation in driving green energy transition[84].

Private sector investment toward a sustainable financial system is by nature diverse and distributed, and unevenly and loosely coordinated. It may also suffer from lack of compliance with federal government policies and commitments. Despite improved regulatory incentives, private sector financing of mitigation and technology change may still be insufficient to catalyze the type and degree of innovation, production and distribution of green energy and green energy technologies necessary to meet Canada's domestic and international obligations[85].

The federal Canadian government is the financial entity best placed to coordinate and to take the necessary financial risks in the development of speculative and yet-to-be developed green energy technologies[86].

Recommendation 6:

> **A New Green New Deal.** ***The federal government should establish a Ministry of Green Energy Infrastructure (MGEI). The mandate of the MGEI will be to design, finance, build, operate and maintain a green energy infrastructure system (GEIF). The purpose of the GEIF is to provide a publicly funded alternative energy system to fossil-fuel generated electricity. The MGEI will promote and coordinate innovation in financing and investment in emergent green energy technologies.***

The financing of the MGEI should initially be through general revenues and other standard public finance techniques (e.g., traditional debt issuance, etc.), but should also be mandated to explore how to create innovative techniques of public finance to fund its research, development, building and operating of the GEIF.

Innovative public finance techniques could include standard financial products, such as issuance of green bonds or debt instruments, but also new forms of finance, such as coordination with the Canadian Central Bank in the creation of long-term forms of finance using distributed ledger technologies to create assets or securities acting as stores of value based on carbon reduction (e.g., “carbon coins”). These financial instrument innovations may be restricted in distribution or be made more widely available where they are consistent with domestic and international climate objectives.

The MGEI will take leadership in the development of the necessary components of a new green energy system, through a publicly funded, owned and operated business that seeks out and invests in the necessary technological development, seeks and employs the required technical, financial and operational talent, and finances the development of these technologies on a national scale.

The federal government (through the MGEI) will be best placed to scale up a green energy system in a manner that is accessible to all Canadians, from industrial production to consumers. It is also democratically accountable to Canadians. There are past examples of state-led development of national-scale industries including electrification, telecommunications and transportation.[87]

Chapter II Conclusion

This Report identifies policy recommendations necessary to the transformation of the Canadian financial market in order to support the transition towards a green economy. It is not only possible but imperative to tilt institutional investors towards greener practices to mitigate the triple-planetary crisis. The Canadian government has the ability and the imperative to drive the sustainable transition to reach its climate commitments, thereby acting in the interest of all planetary stakeholders. The proposal seeks to move away from shareholder primacy, instead highlighting the value and importance of diverse stakeholders including civil society, non-financial organizations, impacted and often exlcluded communities in the Global South, as well as existing and emerging government actors and financial institutions.

The successful completion, and maintenance, of stakeholder primacy and a sustainable financial market is a radical and essential part of achieving the UN's sustainable development Goals by 2030, moving towards net-zero by 2050, and limiting global warming under 2 degrees Celsius as determined by the Paris Climate Agreement. In addition to addressing/tackling the financial sector, one of the most powerful industries in the world, multilateral change as proposed in our recommendations and those of the TBLS working group are imperative.

The connecting link between the propositions is the desire to increase equity across demographics and geographies today. The all-encompassing nature of sustainability radiates throughout industries and issues; 'business as usual' can simply no longer be an

option . The power dynamics between rich and poor and between those few responsible for more climate change than 50% of the world ‘s most disadvantaged populations shouldering the destructive effects of ill-fated, economic policies of growth, extraction, and exploitation require reevaluation, whether it is asset managers fueling financialization, supply chain moguls perpetuating modern slavery or social media giants' use of unsettling and invasive algorithms which further destabilize and undermine democratic processes. As such, the here proposed regulations support increased accountability and justice to promote a radical, and necessary transition towards a more equitable and sustainable Canadian and global society.

Chapter III – Climate Change *changes* Everything

A - Introduction

Chapter 3, *Climate Change* Changes *Everything*, recognises that climate change law is a complex policy arena, with competing claims on profitability, growth, and sustainability. The interdependent challenges of mitigation, adaptation and loss and damage further complicate the debate. If climate change ‘changes everything’[88] at an alarming rate, how can law capture such a task? A critical element underlying effective climate change law is radical institutional and cognitive transformation. Climate change demands a paradigm shift, urging us to rethink fundamental legal and economic systems. To capture the multidimensionality of climate change governance, this chapter examines the responsibilities and complex connections between public and private actors at the national, international, and transnational levels.

Climate change refers to long-term shifts in temperature and weather patterns, primarily driven by human activity since the 1800s.[89] The industrial revolution in the Global North has led to a global economic system which for the longest time focused on growth and consumption.[90] Climate change challenges these assumptions, but current approaches

aim to protect the economic system that caused it. Key problems identified include overconsumption, an overreliance on technological advancement as a primary solution, and the disproportional effect of climate change on the most vulnerable. We propose five concrete recommendations in this chapter that integrate environmental, social and governance factors. They are geared towards a sustainable future with holistic considerations of environmental, social, and governance factors.

B - Literature Review

The world is facing a 'triple planetary crisis' of climate change, nature loss, and pollution and water, where the crises are intertwined and each multi-faceted.[91] In humanity's ongoing efforts to mitigate climate change, it is important to recognize and address the interdependent challenges; otherwise, we risk worsening other crises while claiming to solve one.[92] Public and private actors have taken important steps, such as committing to net zero goals for 2050, but a central concern still surfaces that existing systems and tools are not effective enough given the urgency of the climate crisis.[93]

Developing effective solutions to climate change requires systematic and radical change. The current capitalist economic model that encourages overconsumption is not sustainable. This demands a fundamental shift in how society views economic growth and success, to better incorporate social and environmental pillars. While *Sustainable Development Goal* (SDG) 12 highlights the importance of sustainable consumption, SDG 13 on Climate Action fails to account for excess emissions by the affluent.[94] An individual in the wealthiest 1 percent uses 175 times more carbon than one in the bottom 10 percent. This demonstrates the importance of targeting overconsumption by the wealthy if we are to reach equitable and legitimate solutions.[95] There is also rising consensus that corporations and governments need to place greater importance on *long-term* environmental and social impacts.[96] Case studies such as Latin America's 'Lithium Triangle', in which lithium development is central to a green energy revolution,

demonstrate that the path to green tech may simultaneously place other considerations at risk – thus, holistic assessment is crucial.[97]

What is required is a renewed and sharpened focus on the intricate connections and responsibilities of various actors involved in climate change mitigation: government actors, corporate actors, innovators of technology, and private individuals including the affluent. To ensure effective decision-making, it is crucial to assign shared responsibility for mitigating climate change to all these actors and enhance communication among them.

C - Policy Solutions & Recommendations

Recommendation 1: Environmental Lens - Beyond Net-Zero

International norm-setting bodies, specifically the Conference of the Parties to United Nations Framework Convention on Climate Change (UNFCCC), must redefine climate-related targets to expand beyond emission and temperature targets to better recognize the interdependence of biodiversity, ecosystems, and social inequities.[98] This can be done completely concretely be done through communication between COPs or task forces.

Actors

Targeting nations participating in international bodies enables collaborative discourse between nation-states with degrees of input from stakeholders, like Indigenous peoples and corporations to establish climate, biodiversity, and ecosystem-encompassing norms. Nation-states can then use, and augment, existing legal pathways to set and enforce domestic regulations affecting private actors. Such avenues thus seek to foster strong communication between private and public actors at the international, national, and transnational levels. Additionally, we note that UN bodies like the Task Force on Climate-

Related Financial Disclosure and the Task Force on Nature-Related Financial Disclosure must work collaboratively.

Addressing the Gap

Our current approach to climate change only focuses on reducing emissions by limiting global warming to 1.5ºC by 2030 per the Paris Agreement signed in 2015, a target that even William Nordhaus, the economist who constructed the modelling behind the idea of the target, deems vastly insufficient for achieving an optimal climate and economy.[99] Furthermore, heavy reliance on *carbon dioxide removal* techniques (CDR) has become central to government and corporate net-zero ambitions. CDR compensates for 'overshooting' emissions trajectories,[100] which generally allow for business-as-usual GHG emissions, offset by massive-scale mitigation through unproven CO2 removal technologies.[101] Emissions remain nonetheless embedded as a risk in our environmental, biodiversity, and social fabric.[102]

In the face of this insufficiency, synchronous approaches are needed to accelerate climate change mitigation, while capturing the complex reality that climate change is but one component of the 'triple planetary crisis' of collapsing climate, biodiversity, and waste systems, an idea described by Sara Seck, law professor at Dalhousie University in Canada. Thus, mitigating climate change quickly and equitably is intrinsically dependent on, and amplified by, success in addressing the other two planetary systems.[103]

Obstacles to Overcome

The current international, emissions-based climate regime entrenches rather than rectifies North-South inequality. It exposes specially affected states to the ever-increasing risk and failing to address historic emission and loss and damage.[104] Emissions-based targets need to overcome this equity limitation if we are to achieve *both* a climate, environment, and society that is suitable for human well-being.

Making Impactful Change

According to the Partnership for Environment and Risk-Reduction (PEDRR), incorporating biodiversity and ecosystem-supporting solutions, also known as Ecosystem-based adaptation (EbA), is critical in combating climate change by limiting the impact of natural hazards and reducing the human and economic costs through sustainable ecosystem management.[105]

Expanding the definition of climate change to include biodiversity and ecosystem creates a robust and sustainable future that simultaneously mitigates and defends against the effects of climate change.[106] Strong communication and collaboration are additionally affirmed through Article 15 of the *Kunming-Montreal Global Biodiversity Framework* (GBF), which emphasizes that achieving biodiversity, and by extension climate-forward targets necessitates cooperation and collaboration between national, international, and transnational actors.[107] This includes uplifting and collaborating with Indigenous communities who have been the historical stewards of healthy environments.[108]

Recommendation 2: Economic Lens - Doughnut Overconsume

The financial sector (banks, corporations and governments) must redefine growth in terms of environmental and social pillars, beyond economic. Value must capture the limitations of finite resources to reduce overconsumption by states, corporations, and affluent individuals.

Addressing the Gap

Since the 1990s, governments have recognised the need to respond to climate change, with the first inter-governmental agreement being the United Nations Framework Convention on Climate Change (UNFCCC) in 1992.[109] In this sense, environmental considerations have been pulled into the existing capitalist economic model that is

greatly responsible for overconsumption. The International Panel on Climate Change (IPCC), a United Nations body for assessing the science related to climate change, attributes overconsumption and economic development to climate change.[110] According to Professor Seck, overconsumption continues to be a main contributor to climate change, biodiversity loss, and pollution and waste.[111] The intrinsic link between our economic model and climate change creates the need to find an alternative solution.

Naomi Klein, author of the 2014 book entitled *This Changes Everything: Capitalism vs. The Climate*, has argued that “the idea that capitalism and only capitalism can save the world from a crisis created by capitalism is no longer an abstract theory; it’s a hypothesis that has been tested and retested in the real world”. In other words, the capitalist system that created the climate crisis through the encouragement of overconsumption cannot be the same one to fix it.

Economic growth and increases in gross domestic product (GDP) continue to be viewed as the primary metric of success of an economic system. This view does not take into account the negative environmental and social impacts of the increase in GDP on the environment and communities most vulnerable to climate change.

Obstacles to Overcome

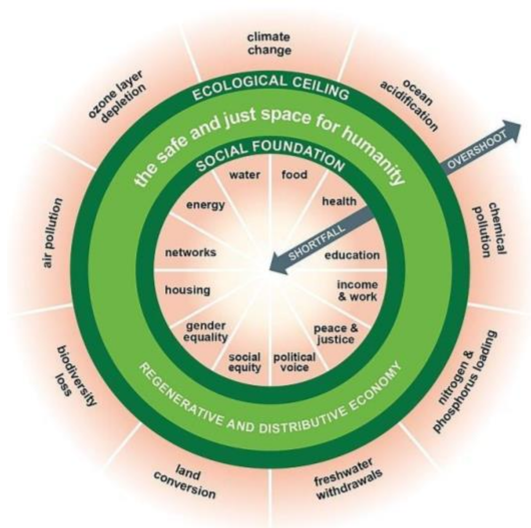
The capitalist economic model is very embedded in our ways of functioning, so a complete change in mindset of the most powerful actors of the financial sector (governments, corporations, and banks) is a daunting challenge. Confronting and contesting this mindset is no small task but one that is essential to ensuring material reduction in negative climate impacts.

Consumption is a key issue that drives climate change, with value being mostly associated with economic and material wealth. This mindset drives consumption by the affluent, who are able to benefit from having global access to goods, services and money. Overconsumption of the earth’s resources by the affluent is an issue that is often

obscured by sustainable development goals which have been criticized for not focusing on reducing consumption targets for the rich.[112] Sustainable development is also thought to require the balancing of economic development, social development and environmental protection each having equal weight.[113] The environment "must be understood as the floor on which society and all economic activity must stand."[114] The obstacles are to cognitively change our way of thinking to address the problems brought on by capitalism.

Making Impactful Change

Our recommendation takes into account the need to recenter the environment and social values within our economic model. For this reason, we support the implementation of the doughnut economic theory, first introduced by Kate Raworth in her 2017 book "*Doughnut Economics: Seven Ways to Think Like a 21st-Century Economist*". The theory takes into account the ecological ceiling to economic growth represented by the outer circle, while the inner circle represents the social foundation.[115] Both circles surround twelve fundamental aspects of life – or the safe and just space for humanity – which can strive for a regenerative and distributive economy. While we recognize that erasing consumption altogether is not possible, we emphasize that this would specifically address **overconsumption** as it remains linked to climate change.



The Report 's working group responsible for chapter 1 outlined the need for corporations to further entrench ESG in their operations by shifting from profit-maximization models to purpose-driven businesses as a first step to long-term sustainable growth, otherwise

known as stakeholder capitalism or, the 'purposive economy'.[116] Similarly, we propose to expand the idea of purpose-driven business to a purpose-driven *economy*, as we recognize that climate change requires an interdisciplinary, multi-stakeholder solution that incentivises real change.

Recommendation 3: Technological Lens - A Piece of the Puzzle

Innovators must prioritize technological solutions that reduce the creation of emissions, not only offset them, and must give due regard to their negative human rights and environmental implications.

Addressing the Gap

The dominant policy response to climate change is to view technological innovation as the solution to offset emissions caused by antiquated, inadequate and inefficient technologies.[117] Relying on technological responses generates complacency and reduces the sense of urgency to tackle the root causes of climate change.[118] For example, framing excess emissions from vehicles as an issue of choice and availability of fuel focuses solutions on the development of cleaner fuels for the future without challenging the excess consumption of fossil fuels which occur today.

In addition, a focus on transitioning to carbon-neutral fuels entails the use of resources, particularly mined minerals and production methods, which bring negative environmental and human rights considerations.[119] For example, Latin American lithium required for electric vehicles poses environmental impacts on land and water ecosystems, as well as the land and cultural rights of Indigenous populations.[120]

Obstacles to Overcome

The push for businesses to adopt 'green' production patterns through the circular economy and zero waste ambitions is an important step to reduce emissions but does

not tackle issues of overconsumption.[121] As noted in Recommendation #1, the reliance on CDR to achieve net zero emissions overlooks that there is little evidence for their success in curbing emissions.[122] For example, nearly 80% of all offset programmes set up under the United Nations Clean Development mechanism have failed to generate a meaningful emissions decrease.[123] Therefore, a mindset shift towards solutions that prioritizes solutions that reduce emissions in the first instance is key.

Making Impactful Change

Innovators of new technology play an important role in our transition to more sustainable systems and in influencing government and corporate ESG policies. Our policy recommendation seeks to acknowledge the important role of innovators while recognising that technology is *a* solution to climate change but not *the* solution. Innovators have the knowledge and skills to create effective technology and to view how policy makers define the problem and how they elaborate and adopt solutions. As emphasized in Chapter 2 of this Report This requires adoption of stronger regulation and transparency requirements by governments and certification bodies on the impacts of market and nature-based technology solutions to climate change, through increased reporting requirements breaking down the material impacts of proposed and implemented technology solutions.

Equally, our recommendation highlights that in any evaluation of a technological solution, due consideration must be given to the technology's impact on other environmental issues and human rights of local communities. The adoption of new technology will always involve trade-offs, which is why a different approach is required. Greater transparency and reporting requirements on the impact of proposed solutions on Indigenous communities and the environment will allow public and private actors to identify the risks associated with different solutions. This will set the stage for the collaborative development of effective procedures of consultation and collaboration with local communities to ensure new industries benefit rather than harm them and their

community. Equally governments and corporations must do more to incentivise innovators to consider the implications for the environment and communities of transition to new technologies, through financial incentives including tax breaks, funding and public-private partnerships.

Recommendation 4: Political Lens - UNDRIP in the Green Transition

Global nations need to participate in implementing the United Nations Declaration on the Rights of Indigenous Peoples (UNDRIP) and must substantively integrate free, prior, and informed consent (FPIC)[124] *for all extraction and development projects, especially when related to the green transition.*

Addressing the Gap

Green transition, a shift towards economically sustainable growth and an economy that is not based on fossil fuels and overconsumption of natural resources, is vitally important in facilitating decarbonization.[125] However when done poorly, as noted in Recommendation #3, resources like lithium and renewable energy required for green transition and climate solutions can be Indigenous rights-violating.[126] Affirming said rights requires robust implementation of the UNDRIP, which sets the standards affirming the rights of Indigenous Peoples. Furthermore, tokenization or simply involving Indigenous participation through consultation is not sufficient, since it does not provide them with the ability to say "no" in the face of unwanted development.[127] Use of FPIC throughout development processes, on the other hand, requires participation that is free from manipulation and coercion, is informed by sufficient and timely information and consent to development that most importantly occurs prior to a decision that affects Indigenous Peoples' rights and interests.[128]

Obstacles to Overcome

Nation-states, however, have been slow to enforce and implement the full spirit of the

Declaration, resulting in green practices that are nonetheless unjust.[129] For example, the Norwegian Supreme Court in 2021 ruled in favour of Sámi activists. In its decision, the Court argued that the construction of turbines without their consent favoured renewable energy infrastructure that encroached on reindeer grazing lands. The Court invalidated the construction permits under the premise that the development was at the expense of their Indigenous rights.[130] Such a finding is, of course, no exception. There is countless, global evidence for the lack of consent and encroachment on, and even damage to, Indigenous environments when pursuing green transitions.[131]

Making Impactful Change

Following the already mentioned Norwegian Supreme Court decision, Sámi communities continue to use the FPIC requirement to contest the validity of other green transition projects that did not receive consent from the Indigenous communities they impact. This is a powerful example of the role that FPIC and other consent-based decision-making processes can have in upholding Indigenous rights. By requiring that *all* nation-states, and by extension their corporations, implement the UNDRIP and FPIC, Indigenous peoples can effectively be a part of the decision-making process and can help avoid potential harms from green transition activities.[132] Nation states must enforce regulations requiring corporations to obtain FPIC prior to development projects.[133] As the known stewards and champions of healthy environments,[134] itis critical to uphold the rights of Indigenous peoples and ensure that they are at the forefront, and can benefit from, the demand for a green economy.

Recommendation 5: Justice Lens - Funding Loss & Damage

A market-share approach must be adopted to fund the Warsaw International Mechanism for Loss and Damage associated with Climate Change Impacts (WIM). Corporations who contribute most to climate change must appropriately compensate those historically and disproportionately impacted.

Addressing the Gap

It is increasingly recognized that particular countries, corporations, and affluent individuals have disproportionately contributed to climate change. The Anthropocene is defined as an era where "humans are now so fundamentally interfering with the biological, geological and chemical systems of our planet, that the effects of these interventions are going to be felt for centuries to come".[135] However, understanding "humans" as the main actors in the Anthropocene is anchored in individual responsibility for climate change and risks ignoring broader disparities in power and responsibilities.

This uneven contribution to climate change exists at multiple levels. The UN Environment Programme reported in November 2022 that "historically, G20 countries have emitted the majority of the greenhouse gases driving the climate crisis", representing around 75% of global greenhouse gas emissions.[136] These emissions have entrenched their economic and political power. In turn, the 'global south' bears the brunt of climate consequences all while constraining their own emissions. The UN Environmental Program reports for example that "Pakistan has seen US$30 billion in damages from severe flooding but emits less than 1 percent of global emissions". These disparities are also seen at individual socio-economic levels as the affluent, particularly the 1%. In February 2023, the International Energy Agency reported that "the richest 0.1% of the world's population emitted 10 times more than all the rest of the richest 10% combined, exceeding a total footprint of 200 tonnes of CO2 per capita annually."[137] Specifically, a 2021 study on inequality by Oxfam, an international charity, identified that "The richest 1% of the global population have used two times as much carbon as the poorest 50% over the last 25 years".[138] As for corporations, major contributors have also been pinpointed. In 2017, the Climate Disclosure Project's Carbon Majors Report identified that 100 companies are responsible for over 70% of GHG emissions.[139] Similarly, in 2023, the Minderoo Foundation's Plastic Waste Makers Index reiterated that "more than half of the world's

single-use plastics waste could be traced directly to just 20 petrochemical companies”.[140]

Obstacles to Overcome

Because “big polluters” can be identified, equal individual responsibility must be rejected. Those who have disproportionately contributed to climate change, must be held accountable as such. The idea that a particular industry can be brought to act on issues of the broader social domain has already been established in many other fields such as health. To name an example, starting in the 1950s, the Tobacco industry utilized the rhetoric of personal responsibility to justify continued production of their product without any constraints to their manufacturer.[141] Litigation and legislative reform against the tobacco industry – particularly cigarette manufacturers – led to big changes in the industry, including : mandatory health warnings, industry-financed public health advertisements, and advertising bans.[142] This Paper proposes that major polluters such as fossil fuel intensive products and services should be treated in a similar manner. For example, in 2022, the city of Amsterdam banned advertisements in public spaces (metro and bus stops) for fossil fuel products and services such as airline tickets and non-electric automobiles.[143] Through increased regulations around consumption and advertising, industries can be brought under public scrutiny if not regulation to acknowledge the need for public protection, even where and, to be sure, because it challenges ‘*business as usual*’. A similar framing may be proposed to push back against individual liability for climate change through concepts such as “carbon footprint”. This term was first coined by British Petroleum (BP) in a 2005 advert which called on individuals to reduce their daily emissions through adopting a range of daily practices, “from washing a load of laundry to driving a carload of kids to school“ without acknowledging the company’s own contributions.[144] Therefore, because Climate Change is an issue inherently tied to the public domain, it “demands collective action on an

unprecedented scale and a dramatic reining in of the market forces that are largely responsible for creating and deepening the crisis."[145]

L&D frameworks respond to this need by identifying who *causes* or *has caused* harm and must be held responsible. This compensation redistributes funds from those who have profited towards those who have been affected by climate change. The Warsaw International Mechanism for Loss and Damage associated with Climate Change Impacts (WIM) was first established at the 2013 UNFCCC COP. "The aim of the L&D Mechanism is to address loss and damage associated with impacts of climate change, including extreme events (such as hurricanes, heat waves, etc.) and slow onset events (such as desertification, sea level rise, ocean acidification, etc.) in developing countries that are particularly vulnerable to the adverse effects of climate change."[146] This highlights the redistributive nature of L&D which acknowledges the particular responsibility of the wealthy, overconsumption, and capitalism rather than the 'universal We'.[147] However, in 2023 Angus William Naylor at the University of Victoria, and James Ford at the University of Leeds, identified a key limitation of the WIM is that the current model does explicitly attribute responsibility.[148] This means that identifying who should finance the L&D system is an essential next step.

In order to address the obstacle of precise traceability of diffuse contaminants such as GHG emissions or microplastics to a particular harm remains, we propose a market share approach. An L&D model anchored in identifying those who *profit* from environmental degradation simplifies the implementability of attributing liability/responsibility. A market share attribution of tortious liability was notably seen in the 1980 US case *Sindell v. Abbott Laboratories.*[149] In *Sindell*, multiple pharmaceutical manufacturers were jointly sued and, ultimately, held responsible for producing harmful drugs. The exact manufacturer of the prescription taken by an individual victim could not be traced meaning no single wrongdoer could be identified as responsible for a specific injured party. To remedy this uncertainty in causality, the court found that "[e]ach defendant will be held liable for the

proportion of the judgment represented by its share of that market" to increase accountability.

Therefore, since it is impossible to identify exactly which emission or which microplastic, let alone which manufacturer or emitter, causes a specific harm, a market share liability identifies corporations as a key actor responsible for funding L&D. In addition to market responsibility, the WIM could also evolve to call on states to apportion special funds. These could be collected through fines and penalties to the L&D system. For example, when a corporation is found to have been engaging g in greenwashing, these funds should be allocated directly towards green initiatives rather than being channelled towards a general spending pool. Again, this responds to a central limitation of L&D because it increases sources of funding by holding the appropriate corporate actors responsible.[150]

Making Impactful Change

Once this approach is implemented to ensure proper funding of the L&D compensation, further attention can be turned to the exact distribution of funds towards marginalized communities and projects that further advance environmental justice. Identifying the concrete ways in which this capital is spent will underline the redistributive nature of L&D as a remedy. For example, ongoing considerations include how to compensate broad stakeholders including marginalized communities, and also future generations or nature itself.[151] Echoing this paper's first recommendation, this approach must be inclusive of all environmental harms, including biodiversity. This reflects recommendations from the *International Institute for Environment and Development* (UK) and the *International Centre for Climate Change and Development* (Bangladesh) to incorporate biodiversity as part of the WIM framework to account for harms beyond climate catastrophes.[152] In short, once funding is secured through a market share approach, transparency will remain imperative

to ensure compensation is provided to green initiatives all while empowering marginalized views.

Chapter III Conclusion

A common thread in all chapters of this policy paper is the Authors' emphasis on th the need for an approach that highlights less dominant viewpoints and incentivises effective change. This chapter has aimed at expanding the recommendations of Chapter 1 and 2, whereby corporations must develop uniform ESG standards to increase transparency and accountability. In support of these recommendations we have argued that to effectively combat climate change requires a fundamental institutional and cognitive transformation, jointly enabled by private and public actors. Specifically, governments and corporations, as they incorporate technological and human rights considerations, have the onus for reparative and forward-thinking economic reforms to drive decarbonization in an age of unsustainable overconsumption.

This chapter has identified a number of key recommendations towards a more sustainable future: climate change mitigation targets must expand beyond emission targets to better recognize the interdependence of ecosystems and social inequities, and growth must be defined beyond its traditional economic framework to environmental and social considerations. Technological solutions that reduce the creation of emissions should be prioritized over those that merely offset. Marginalized voices must be better accounted for in decision-making, and Loss and Damage remedies must be adequately funded.

These cognitive shifts reinforce this paper's earlier recommendations regarding transparency and accountability to provide a firm foundation on which the following chapters' recommendations for tackling modern slavery in global supply chains and artificial intelligence can be understood.

Chapter IV – Global Value Chains

How can we reconcile the "value" of global value chains with the protection of human rights?

Global value chains ("**GVCs**") benefit from the differences between jurisdictions that lead to their respective comparative advantages. These advantages can be based on natural resource availability, technological advancement, or regulatory differences. However, in their search for greater profits, corporations have taken advantage of differences in labour standards and their enforcement which often contravene human rights. This has paved the way for an environment that enables the continuation of modern slavery. In an attempt to balance profitability and the protection of human rights, this chapter explores how we can reconcile the use of GVCs while eradicating modern slavery.

Previous attempts at regulation focusing on transparency have proven inadequate. Trust in corporate self-regulation has faltered. Our primary focus therefore will be on regulators, as the current complacency of corporations contributes to the perpetuation of modern slavery.

A - Defining the Problem

Today's global economy is largely structured by interlocking and multi-tiered global value chains. The concept of GVCs refers to the phenomenon that international production is organized through a division of labour between many companies, relying on activities and tasks carried out in different countries.[153] These value chains exceed territorial borders of nation states and are characterized by linkages between different corporations. Instead of multinational companies operating on a global scale, firms rely on a complex network of affiliates, contractual partners, and suppliers.[154]

Today, a single finished product often results from manufacturing and assembly in multiple countries, with each step in the process adding value to the end product.[155] This raises two key questions. The first relates to how the economic value from the sale of these goods and services gets distributed among nations, companies, and individuals throughout a GVC. The second, which has received less attention, relates to what forms of non-economic value are not, and should be, recognized by GVC governance.[156] For instance, the quality and nature of jobs created in the chain could also be viewed as value creation, as is the degree to which the GVC minimizes its environmental impact. Further, in the context of the COVID-19 pandemic and associated supply chain disruptions, resilience and risk management are also increasingly being identified as important considerations in supply chain governance.[157]

While corporations benefit from GVCs and operate transnationally, human rights protection and enforcement are still stuck in the logics of nation states. This has led to a gap in the effective control of corporate operations and their compatibility with even basic human rights such as freedom from slavery. The first Global Slavery Index was produced and published by Walk Free in 2013. They defined modern slavery as a practice that encompasses human trafficking, forced labour, slavery and slavery-like practices.[158] The need to act against modern slavery has never been so urgent: 49.6 million people are still enslaved worldwide.[159] The inadequacy of focusing on state obligations to protect human rights has entered public discourse for a long time. However, from a corporate perspective, the field is still in its infancy.

B - Defining Stakeholders

Multinational corporations are integral to globalization and GVCs are understood as networks of corporations with varying levels of integration.[160] *International and supranational agencies* such as the United Nations (“**UN**”) are norm-setting organizations

for states who frame the conversation on modern slavery and also set the targets and goals that are to be met. For example, with "Sustainable Development Goals (SDGs), the global community has committed to ending modern slavery among children by 2025, and universally by 2030."[161] *International NGOs* can have standing against corporations regarding their acts and treatment of others within the GVC and can attempt to identify corporations that are not in line with human rights or modern slavery legislation in a given jurisdiction. For example, a workers' union in tandem with two NGOs filed the first complaint under the new German due diligence law.[162]

Domestic stakeholders are the various actors at the domestic level who are involved or have an interest in ending modern slavery. *State governments* have an interest in ensuring that the human rights of their citizens are being protected, and that they are not being exploited via modern slavery. However, specific governmental departments are implicated and involved in addressing the issue more than others. For example, in the United States, the Department of State (equivalent to other countries' ministry of foreign affairs) has pioneered the Program to End Modern Slavery (PEMS).[163] *Domestic corporations* also play a significant role in issues related to modern slavery and human rights. The level of direct involvement in this issue is highly dependent on the jurisdiction in question. Social factors (e.g., cultural or traditional norms) can affect the persistence of modern slavery in the supply chain, as can geographical features such as physical remoteness, and economic features such as a high proportion of low-skilled workers.[164] *Lobby groups* may push for an agenda of decreased oversight, or instead advocate both for increased accountability for modern slavery and exploitative practices. The specifics vary by country; however, the UK's experience with the creation and implementation of the 2015 Modern Slavery Act as well as California's 2010 transparency in global supply chains legislation provide illustrative, early examples. Today the field is much more crowded of course with remarkable levels of diversity when it comes what is being scrutinized as 'disruption'.[165] Industry players emerged as formidable opponents lobbying

against heightened oversight measures. *Distributors* are conduits between multinational corporations ("**MNCs**") and suppliers in GVCs. *Workers and workers' unions* can help represent the individuals on the ground. *Consumers* are directly and indirectly implicated in modern slavery.

C - Defining Current Approaches and Their Limitations

Two regulatory approaches that have been adopted to combat modern slavery are transparency legislation and human rights due diligence ("**HRDD**") frameworks.

The transparency approach is exemplified by the *California Transparency in Supply Chains Act* of 2010*,* which forces companies to publicly disclose their efforts to eradicate modern slavery within their supply chain. Similar transparency-focussed legislation include the *The Slave-Free Business Certification Act* of 2022 in the United States, the already mentioned *Modern Slavery Act* of 2015 in the United Kingdom, and the European *Corporate Sustainability Reporting Directive* of 2022. Canada's *Fighting Against Forced Labour and Child Labour in Supply Chains Act,* formerly known as Bill S-21, has been assented in May 2023. The primary objective of transparency legislation is to ensure that corporations recognize the impact of their activities on sustainability, and conversely, how sustainability impacts their operations and overall organization.

We are witnessing a progressive shift from transparency-based legislations to binding HRDD frameworks. Primarily emerging in Europe, these legislations focus on imposing substantive requirements for companies to uphold human rights within their GVCs. Examples of such legislations include Germany's Supply Chain Due Diligence Act (SCDDA) of 2021, France's *Loi sur le Devoir de vigilance* of 2017, and the proposed European Union directive by the European Commission in 2022. These regulations impose obligations on corporations by primarily adopting a managerial approach. They mandate parent companies to establish codes of conduct that encompass preventive

measures against human rights violations. These binding preventive actions draw inspiration from soft international standards, especially the so-called “Ruggie Principles” which emphasize, (i) the duty of states to protect human rights, (ii) the responsibility of companies to respect human rights and to comply with all applicable laws, and (iii) those affected by human rights violations must be granted appropriate and effective access to remedial options[166]. The objective of these preventive actions is to identify and mitigate risks throughout a company's value chain, including both commercial (contractors and subcontractors) and capitalist relationships (subsidiaries). However, while this responsive approach primarily aims at the protection of workers and individuals from severe rights violations, it remains largely insufficient.

Despite the genuine will of some regulators to tackle the modern slavery and human’s rights issues in the GVC, some major improvements still need to be made.

D - Proposed Recommendations

Recommendation 1: Mandating Visibility

We recommend that regulators should mandate value chain visibility, e.g., adoption of blockchains in order to improve traceability within global value chains.

Many corporations do not themselves truly know the various suppliers that are involved within their supply chain tiers. For example, many North American retailers source from China, and other regions in Asia, via distributors and therefore do not have direct access to suppliers and producers of input goods.[167]

Blockchain-based technologies have been proposed as a potential solution. Blockchain is a crowd-sourced information computing system, which can be used as a digital ledger

to record transactions and exchanges in a supply chain.[168] Each participant in the blockchain network has a unique digital signature. The cryptographic keys used across the shared ledgers provide a history of all the transactions on the blockchain, which can address transparency issues.[169]

Despite the emergence of these new technologies, rollout of traceability initiatives within supply chains has been slow due to a variety of reasons including substantial adoption costs. Moreover, the lack of operational expertise, technical infrastructure as well power politics and international standard-setting may also pose problems.[170] Even when companies have embraced traceability, this data is often commercially sensitive and corporations may wish to protect their competitive advantage.[171] Thus, the present approach of leaving the issue of supply chain transparency largely in the hands of the corporation is insufficient.

Therefore, regulators must incentivize and mandate the adoption of value chain traceability to ensure visibility of the human suffering present within GVCs to consumers and investors. To balance the legitimate privacy concerns of corporations with transparency needs, the information can be decentralized and accurate. The regulators must therefore also ensure that the information of corporations is sanitized.[172] The system used must be industry agnostic in order to maximize the commercial utility of the system. It also must be based on the global supply chain information standards.[173] Recent developments in blockchain technologies and management could present such an avenue. For instance, Glew, Tröger and Schmitter (2022) have proposed a prototype solution for anonymous sharing in a complex supply network.[174] Going forward, such solutions could serve as effective tools to monitor provenance data and to provide verifiable information on the production processes used in global value chains.

Recommendation 2: Re-centering Human Value

We recommend that government regulators consult affected foreign actors when drafting legislation and considering the governance of global value chains.

Re-centering human value within GVCs is essential because the discourse often focuses on products and profits while disregarding the individuals most affected.[175] Historically marginalized communities who often have fewer labour protections are those most impacted by modern slavery.[176] Lead corporations exploit this unfair reality, taking advantage of conditions such as low wages, class disparities, and inadequate legal safeguards for workers.[177] Moreover, multinational corporations and their home countries continue to reap benefits from the absence of enforced human rights protections within GVCs. This inequality is rooted in the broader global economic disparities with historical origins in colonialism.[178] Consequently, GVC regulations established in Global North countries have faced criticism for their extraterritorial impact on host countries and their failure to incorporate input from Global South countries and affected workers.[179] To bridge this gap, our recommendation aims to address the disconnect between those being regulated, those experiencing the impact, and those involved in decision-making processes.[180]

Government regulators in the countries where lead companies are located should collaborate with local governments and trade unions or employee groups during legislative drafting and implementation**.** This approach enables government action to be informed by existing movements prioritizing workers rights and economic concerns.[181] Further, this approach can be pursued by individual countries implementing GVC regulations, as it does not require the oftentimes slow process of developing multilateral agreements. This recommendation should be implemented through at least an equal number of actors being consulted from host and home states. Additionally, there should

be ongoing dialogue with relevant host country governments and organizations to ensure regulations are effective and amend them as needed.

This ensures that individuals affected by human rights abuses, and countries where these abuses occur, are no longer excluded from GVC governance.

Recommendation 3: Access to effective legal remedies

We recommend that regulators ensure that victims have standing in courts to access effective legal remedies and implement a reversal of the burden of proof.

We observe that victims of GVCs have for years been struggling to access effective legal remedies in the courts of the home states of lead firms. This struggle is the result of the mismatch between the transnational nature of GVCs and nation-state based jurisdictions, in combination with the fact that private international law rules do not address, let alone accommodate this mismatch. As a direct consequence, victims face procedural barriers, amongst which is a lack of standing to claim remedies against a lead firm.[182]

The effects of any change to the substantive law of a home state will depend on the rules that determine the jurisdiction and the applicable law in a particular case. Whilst the former issue - jurisdiction - seems to have been settled to the benefit of courts in home states having jurisdiction[183], the latter - applicable law - is still uncertain. Usually, in transnational litigation, the law of the place of damage applies. This rule renders any change in the substantive law of home states irrelevant.

Moreover, Klaas Hendrik Eller, from the Amsterdam Center for Transformative Private Law, notes that "global value chains use contracts as central building blocks"[184]. These contracts often include human rights and environmental obligations. Yet, those directly

affected by a breach of contractual provisions on human rights and the environment - workers and communities – do not usually have standing to bring a claim against the involved firms because they are considered as third parties. And as law professor Diamond Ashiagbor of the University of Kent reminds us, the structural connections between the use of disempowered, racialized foreign labour in the colonies and the exploitation of salaried workers and the "invisibilisation of women and their work" in the Global North move supply chain governance questions from the periphery into the centre.[185]

Another reason for the insufficient legal protection of victims is the difficulty victims face in proving the causal link between a harm that occurred in a foreign country and the harmful conduct of a lead firm. This remains the case also under the HRDD legislation being adopted in different countries.[186] In the absence of a reversal of the burden of proof, victims need to prove that the parent company failed to take preventive and reasonable measures to avoid the damage. This is even more difficult in light of the fact that the legislation lacks a clear definition of what 'preventive and reasonable' measures entail in the context of human rights due diligence. As seen in France, even the judge struggles in understanding what is a reasonable preventive measure, leading to a presumption of irresponsibility for lead companies, and letting the victims without any solution to be compensated.[187]

The first step to address the just-mentioned obstacles must inevitably consist in facilitating victims' access to courts of lead firms' home state jurisdictions. Effective access to justice depends on money and know-how, which are two resources that victims of human rights violations in GVCs often lack. In that regards, Germany's new *Supply Chain Due Diligence Act* includes a note-worthy provision on the special capacity to sue for NGOs (§ 11 of the Act).[188] The Act allows claimants to authorise NGOs and unions to represent them in civil claims. As representatives of victims, they can file a complaint for

damages and litigate the claim in their clients' best interests. The legislator should consider a similar provision to ensure that victims can capitalise on transnational advocacy networks in order to bring their claims in the home state jurisdictions of lead firms.

Secondly, in order to further ease the access to an effective remedy, state regulators should consider a change in the burden of proof. Under current laws on evidence, the burden to prove the legal conditions for civil liability is on the claimants. However, it is often the company, and only the company, that possesses the necessary knowledge and documents to demonstrate that these conditions have been met. An illustrative example consists in the showcasing of a duty of care relationship between the lead firm and the affected third parties. As manifested in the widely noted decision *Vedanta Resources PLC and another v Lungowe and Others*[189], the UK Supreme Court considered competing claims on jurisdiction and on corporate accountability for egregious human rights abuses in the parent's subsidiary. Claimants had to prove (and successfully did) the existence of a prima facie close relationship between the lead firm and themselves. In order to do so, they drew on publicly available sustainability reports and other corporate documents. However, the court will in the merit stage (the case is still ongoing) determine whether that close prima facie relationship had indeed existed. Only the internal corporate documents of the company in question can provide a definite answer to that question.[190] In order to address that imbalance between the burden of proof and the access to the information to fulfil that burden, state regulators should consider a reversal of the burden of proof by introducing a presumption of a lead firm's control in GVCs. Such a presumption shifts the burden of proof to the company to show that, in a specific case, it did not have the control and would thus not be liable.

A third, overarching issue that has arisen as regards the access to effective remedy is that of the applicable law. A court in a home state jurisdiction can only consider any new legislation on human rights due diligence – such as for example a reversal of the burden

of proof as suggested above - if the applicable law is that of the home state jurisdiction. The following case should serve as an illustration: In *Jabir and Others v KiK Textilien and Non-Food GmbH Regional Court (Landgericht) of Dortmund,* a survivor and three family members of victims of textile factory fire in Pakistan in 2012 that killed over 260 people[191] filed a lawsuit against KiK, a German clothing retailed at the regional court of Dortmund, Germany. In 2019, the court rejected the lawsuit arguing that under the Pakistani law on physical harms the statute of limitation of one year had expired[192]. As the court had determined Pakistani law to be the applicable law, there was no room left to consider the incidence and potential liability in light of the human rights due diligence discussion that had already been underway in Germany.

Hence, in line with our recommendation on the re-centralising of human value, and visibilising the real costs of GVCs, we suggest including a provision that leaves it up to the claimants to choose the applicable law in a particular case. Article 7 of the Rome II European Regulation already includes such a provision for environmental damages. It states that the law applicable to torts arising out of environmental damage shall be the law of where the damage occurs, unless the person seeking compensation for damage chooses to base his or her claim on the law of the country in which the trigger event occurred.[193] In order to enable effective legal remedies, a similar exception rule for the case of human rights violations in GVC should be created. In that way, victims could choose the law that is more favourable to their case.

Recommendation 4: Collaborative Certification Regime

We recommend that regulators and NGOs co-create a certification, tied to financial incentives, recognizing companies that do not use slave labor in their supply chain.

As discussed earlier, there is a natural tension between the protection of human rights and the profit motive within GVCs. Regulators must adopt a "carrot and stick" approach, i.e., offer incentives and disincentives to encourage corporations to eradicate modern slavery in their supply chains. One approach would be the implementation of stringent and widely recognized certifications. Although some certification models exist to encourage businesses to enhance their social and environmental practices, there is currently no direct certification specifically aimed at recognizing companies that successfully eliminate modern slavery from their supply chains.[194]

We recommend the establishment of an NGO-led certification process to guarantee that companies do not use slave labour. However, a major concern with such certification regimes is the possibility of "label proliferation"[195] resulting in consumer confusion and ignoring the labels entirely. There is also a risk of "NGO capture" (whereby NGOs may be influenced by powerful corporate actors) which may lead to less stringent standards.[196] To address these concerns, we recommend that the certification process should undergo annual approval and verification by the government. This rigorous oversight will enhance the certification's credibility. Independent analyses and assessments should be conducted to thoroughly evaluate the company's operations on the ground. This novel collaborative approach between NGOs and regulators is aimed at bolstering the certification's legitimacy and establishing it as a trustworthy indicator of a company's commitment to eradicating slave labor.

Additionally, we propose linking this certification to financial incentives for the certified companies, akin to the approach taken with the B Corporation certification. Companies holding this certification to confirm their supply chains are free of modern slavery would be eligible for enhanced financial benefits from institutions like the Business Development Bank of Canada (BDC). These benefits could also include access to

competitive loans and grants, as these certified companies are deemed to present lower risks for investors.[197]

Public and private banks, investors, and other financial institutions can extend more favourable loans, rates, and credits to companies that have obtained the modern slavery-free certification. By doing so, these institutions recognize the reduced litigation and reputation risks associated with such certified companies. Thus, this certification can serve as a strong incentive for companies to proactively eliminate slave labor from their supply chains and actively contribute to the protection of human rights within GVCs.

Recommendation 5: Increased policy coherence and ending the siloed approach to addressing modern slavery

We recommend increasing policy coherence by adopting a "whole-of-government approach" and combining the above recommendations into one multi-pronged strategy so as to close existing policy gaps.

What is clear from the recommendations above, and from prior attempts to design solutions to the persistence of modern slavery in GVCs, is that no one solution on its own is sufficient. Efforts have been made to improve visibility and monitoring, but these interventions have been piecemeal and mostly voluntary.[198] There have been attempts to design new laws, but these have had significant limitations.[199] Incentives have been effective in certain limited cases, but not strong enough to drive systemic change[200]. Finally, the voices of those most affected continue to be excluded from the debate and therefore lack the major social influence required to drive change[201]. The shortcoming of these approaches, then, is not that they are entirely ineffective, but rather that they cannot work in isolation. Coherence between these interventions in the form of a coordinated and multifaceted approach is thus critical if any of these are to truly address human rights abuses in the global value chain.

What we envision is an approach that looks something like the following. We know that we need to design new legislation that would show states' desire to eradicate modern slavery and would address current issues with standing, so that people may bring actionable claims against corporations who continue their exploitative practices. However, such legislation will be ineffective if we do not have technology-driven improvements in visibility and transparency, such that governments and consumers can truly understand where products are being produced and the truth of what is happening in those locations. Corporations will not implement such technology, however, if they lack strong financial incentives to do so. After all, corporations are driven largely by the bottom line and their need to generate profits. Legislation must thus be designed to incentivize companies to implement these visibility mechanisms and penalize those that refuse to comply. For such legislation to have the required popular support in a democratic governance system, citizens must better understand the moral dimension of this issue: those who have experienced modern slavery must be given the space to tell their own stories and advocate for their own solutions.[202]

In this way, rather than suggesting several independent interventions, what we are really proposing is a whole-of-government approach[203]: we must implement each aspect of these interventions in tandem so that they complement each other and close off the gaps that currently exist in the modern slavery regulatory regime. After all, it is due to these gaps that modern slavery continues to flourish, despite the fact that the vast majority of people are in agreement that modern slavery is a moral travesty and has no place in today's world. Implementing such an approach would be well-aligned with the United Nations Guiding Principles on Business and Human Rights, which state that ensuring both vertical and horizontal policy coherence is critical to helping states manage both the business and human rights agenda.[204]

Chapter IV Conclusion

The world is increasingly globalized, and a direct consequence of this is that corporations are able to hide the exploitation of individuals and their labour deep in GVCs. We have proposed a comprehensive set of solutions to address these issues. However, we also recognize that this issue does not exist in isolation. Our focus on shifting global value chains away from a singular focus on cheap production is mirrored in chapter one's emphasis on the broader need for corporations to prioritize social purpose over profit. By integrating this perspective into both corporations and the global value chains they participate in, meaningful globally change can be created. Further, the second chapter's focus on sustainable finance requires the integration of sustainability into every aspect of financial decision-making. This is a highly complex and hard to implement endeavour that chapter two's recommendations seek to address, just as this chapter grapples with the difficulty of governing global value chains. Further, this chapter's efforts to reconcile the benefits of global value chains with their significant human costs raises questions similar to those addressed by chapter three in its analysis of the implications of climate change. That chapter's focus on the impacts of consumption as well as the distribution of economic benefits and human harms may imply a more restrained role to economic production throughout value chains or a re-assessment of how value chains impact workers through the intersection of climate change and human rights. Finally, just as global value chain governance requires companies to take responsibility for how they are sourcing their inputs, and be held accountable for failing to do so, chapter 5 will outline their central role in the responsible curation and moderation of public digital spheres.

Chapter V: Corporations and Democracy in the Age of Digitization and AI

A – Introduction

Digitization and artificial intelligence (AI) are fundamentally transforming the manner in which social interactions, material production, and knowledge generation take place. With the increasing availability of data, predictive algorithms, and artificially intelligent systems, individual and societal patterns of behavior have become commodified and tradable assets in the financialized economy. As such, tech and platform corporations have become social, economic, and political rulers and arbiters. These circumstances have created new considerations for Canadian law stemming from a series of burgeoning regulatory concerns, including: how AI contributes to or alleviates existing social and political tensions, how biases and issues of ownership shape technological and economic conditions, how AI can simultaneously contribute to and alleviate issues with corporate governance and democracy; and why AI *regulation* is needed in order to uphold corporate social responsibility and the purpose-driven economy.

Developing a transformative framework to address the increasing interaction between AI, corporations, and democracy is challenging, however, because AI lacks a widely accepted definition, despite its increasing social prevalence. Any definition and regulation of artificial intelligence will cement new apparatuses of control now and into the future, with potentially serious repercussions for corporate and economic growth and democracy.

To address regulatory gaps while seeking to uphold principles of democracy and social responsibility, this Chapter looks to regulate *Very Large Online Platforms* (VLOPs) and their use of AI and algorithmic systems to curate, amplify, and moderate divisive,

polarizing content. Regulatory frameworks for corporate social responsibility must include considerations about VLOPs' use of AI and algorithmic systems because those platforms are digital public spheres where political opinions are formed. By being socially responsible, corporations can strengthen their brands, increase market share, reduce operating costs, innovate, and remain competitive.

Through the implementation of broad transparency and accountability measures, including a mandate for responsibility-by-design measures, this Chapter moves towards the goal of holding clearly identified creators, controllers, and owners of AI and algorithmic systems to account.

B - Literature Review

Contextualizing the Problem

VLOPs have become a key site of democratic debate, discussion, and political opinion formation. However, Canadian principles of democracy are directly threatened by the increasing spread of misinformation and disinformation on VLOPs. Democratic societies tend to make decisions based on an understanding of the world that is represented through and by different media. In the last decade, digital platforms like Facebook/Instagram, Google/YouTube, Twitter and, to a certain extent, TikTok, have supplanted traditional publishers and broadcasters as a primary means for distributing information. These new media platforms have not maintained the same information standardization practices as the legacy media institutions they are increasingly replacing.[205] This disruption has allowed commercial and political motives to overshadow – to an even greater extent than before – the public's interest in fair and accurate information.

Rosenberger's work,[206] for example, draws attention to the use of VLOPs by authoritarian governmental regimes in an effort to control national information spaces

and advance certain geopolitical and economic goals. These tactics gained significant traction in the wake of Donald Trump's 2016 presidential campaign, wherein Russia's efforts to manipulate election outcomes resulted in: 1) flooding of VLOPs with "fake" content; 2) altering of users' search results; 3) amplification of extreme and polarizing narratives; and 4) the spread of hacked and weaponized information via mainstream VLOPs. It is within this context that a growing number of researchers, scholars, and civil society actors have begun to view "bad faith as the condition of the modern internet."[207]

What's more, the business models of VLOPs tend to reward the platforming of sensational mis- and dis-information because they depend upon maximal levels of user engagement to increase revenues.[208] This push towards attention maximization devalues civil deliberation and participatory democracy by profiting from users' conflict, outrage, and harm. It fragments audiences and causes users to tribalize into macro- and micro-identity formations that become further niched in both on- and off-line contexts. In fact, a growing body of research has shown that defining characteristics of online political communication, including targeted advertisements, interactive live video options, and emoji "reacts," on the Facebook News Feed are uniquely suited to facilitate psychological processes of polarization.[209]

Content curation yields tremendous power for VLOPs to influence and reinforce its users' beliefs, creating personalized echo chambers. Mis- and dis-information curated according to users' data history and political profiles can push users to the fringes of the political spectrum. This is especially the case for mis- and dis-information that is designed to elicit strong emotions and legitimize extreme beliefs by acting as evidence supporting extremist ideologies.

Content Moderation

VLOPs like Facebook/Instagram, Google/YouTube, and TikTok routinely screen and make decisions about the content being shared on their platforms. This practice is referred to as "content moderation." Since 2016, content moderation has become a top

priority for VLOPs and a central concern for law/policymakers, governments, and civil society actors. However, forms of content moderation have existed since the conception of online communication. In the early days of the internet, content moderation was undertaken by volunteers on a peer-to-peer basis.[210] For this reason, recommendations about content moderation policy tend to concern the nature of moderation (human or AI) and the corporate/commercial decisions that organize how content moderation is structured and carried out.[211]

The lack of effective content moderation of mis- and dis-information allows for the widespread propagation of fake and misleading content on VLOPs. Research released on October 12, 2020 from a group of American social media analytics firms[212] found that the number of likes, shares, and comments on fake and misleading content on Facebook increased three-fold from 2016 to 2020.[213] As such, VLOPs can certainly be conceptualized as key locations for the spread of mis- and dis-information that, in turn, can sway political opinion and voting behavior and thus affect the state of democracy in Canada and abroad.

The use of AI systems to screen user-generated content and to determine whether that content is acceptable has been increasing in the last decade.[214] Problematic, though, is that these AI systems cannot accurately screen all content, including those that feature mis- and dis-information. On Facebook alone, AI systems report around three million items for potential removal per day.[215] Facebook's CEO, Mark Zuckerburg, noted in a November 2018 White Paper, however, that AI moderators make mistakes in more than 10% of cases. This suggests that 300,000 content moderation errors are made every 24 hours on Facebook – one VLOP – alone.[216] Due to the sheer amount of content that circulates on VLOPs, seemingly low error rates can still lead to the large-scale spread of mis- and dis-information that has the potential to undermine democratic values.

The offline effects of widespread mis- and dis-information can be illustrated by the 2022 'Freedom Convoy' in Ottawa, Ontario, where hundreds of vehicles rallied at

Parliament Hill to protest COVID-19 vaccine mandates and restrictions.[217] During the COVID-19 pandemic, various forms of mis- and dis-information propagated VLOPs. Claims that the Canadian government and the media were lying about the severity of the pandemic and that the COVID-19 vaccine was unsafe helped fuel the protests.[218] This is but one example highlighting how VLOPs' content moderation practices may impact peoples' political, social, and economic ideologies, which can sway voting behaviors, threaten the quality of public debate and deliberations, and potentially compromise fair and transparent electoral competition. These issues must be addressed in order to maintain democratic stability – the bedrock of social and economic flourishing. Only then can corporations, including VLOPs, meaningfully fulfill corporate social responsibility mandates.

Regulatory Landscape

Artificial Intelligence Policies

As part of its re-introduced privacy legislation, the Canadian Government outlined a new regulatory framework to govern AI systems: the *Artificial Intelligence and Data Act* (AIDA). Its central objectives include: 1) the regulation of international and interprovincial trade and commerce in artificial intelligence systems; and 2) the prohibition of certain conduct in relation to artificial intelligence systems that may result in serious harm to individuals or harm to their interests.[219] While the legislation aims to prompt better industry standards and oversight, some profound harms related to AI require a much more robust legislative framework for accountability. In particular, the draft delegates responsibility for conducting and using AI technologies to industry actors and does not call for or create the scaffolding to implement independent regulatory oversight.

Other legal norms to consider are enacted under EU legal frameworks, including the *AI Regulation Proposal* and the *Directive Proposal on AI Responsibility*. The *AI Regulation Proposal* proposes three categories to regulate AI systems depending on the risk that those systems pose to the EU: (i) an unacceptable risk, (ii) a high risk, and (iii) a

low or minimal risk.[220] An unacceptable risk is one that, for instance, "…covers practices that have a significant potential to manipulate persons through subliminal techniques beyond their consciousness or exploit vulnerabilities of specific vulnerable groups such as children or persons with disabilities to materially distort their behavior in a manner that is likely to cause them or another person psychological or physical harm."[221] Practices entailing an unacceptable risk are explicitly forbidden. Conversely, high-risk systems can operate in the EU, "'subject to compliance with certain mandatory requirements and an ex-ante conformity assessment."[222] Two main categories fall under the high-risk label: AI systems intended to be used as safety components of products subject to third-party ex-ante conformity assessment, and other stand-alone AI systems with mainly fundamental rights implications.[223] Annex III prescribes a list of AI systems whose risks have already materialized or are likely to materialize soon.[224]

In terms of transparency, the EU *AI Regulation* is notable because it imposes a general transparency obligation on providers to ensure that AI systems intended to interact with "natural persons are designed and developed in such a way that natural persons are informed that they are interacting with an AI system unless this is obvious from the circumstances and the context of use."[225]

An additional relevant regulation to scrutinize in the AI regulatory context is the *Canada-United States-Mexico Agreement* (CUSMA) which acknowledges the importance of "interactive computer services" for small and medium-sized companies to the growth of digital trade within the transnational relationships of the three countries.[226] Notably, the international treaty establishes that American, Canadian, and Mexican legal regimes cannot hold VLOPs liable for the information broadcasted on VLOPs operating within them.[227]

Conversely, countries such as China and Thailand operate under strict liability regimes, wherein platforms are held responsible for third-party content. Conditional liability regimes offer platforms immunity on the condition that they adhere to prescribed

procedures. Notice-and-takedown regimes like the U.S. *Digital Copyright Millennium Act* (1998) fall under this category, requiring that platforms remove content upon receiving a notice of infringement. Under broad immunity models, intermediaries are not held liable for third-party content.

Content Moderation Policies

Generally speaking, there are two broad categories of content moderation: 1) symptomatic and 2) structural. The first category considers policies designed to specifically target hate and harmful speech that has been published by users onto platforms.[228] These policies are all *ex-post* in that they identify, take down, and potentially punish the posting, publication, or circulation of speech *after* it is posted online.[229] The second category of policies, *ex-post* policies, addresses the structural causes of online harm and hate speech.

The German Network Enforcement Act (NetzDG) imposes heavy obligations both *ex-post* and *ex-ante* on VLOPs for their content moderation practices. Not only does it impose mandatory public reporting, it also compels VLOPs, under a penalty of up to five million euros, to remove "manifestly unlawful" content within 24 hours and borderline content within seven days.[230] This strong moderation obligation might be acceptable within the German policy context, where freedom of speech is narrower than in other countries, but it still raises significant concern for possibly violating "Germany's obligations under European human rights law."[231] This law can therefore be seen as an illustration of the excess of moderation and how it could, while pursuing a legitimate objective, become a danger for liberal democracies.

Other countries use pre-existing legislation or are proposing new ones to address the use of AI for content moderation by VLOPs. In the U.S., for example, Section 230 of the *Communications Decency Act*, otherwise known as the "net neutrality" law, provides that "no provider or user of an interactive computer service shall be treated as the publisher or speaker of any information provided by another information content

provider."[232] However, the proposed *US Filter Bubble Transparency Act* requires "that internet platforms give users the option to engage with a platform without being manipulated by algorithms driven by user-specific data."[233] Therefore, this proposal would introduce new *ex-ante* obligations.

C - Policy Recommendations

The following recommendations apply to Canadian VLOPs that use AI and algorithmic systems. Notably, these include: Facebook and Instagram, Twitter, and TikTok.

Recommendation 1: Accountability

Algorithmic Impact Assessment (AIA): VLOPs shall complete the risk assessment mandated under the Canadian Directive on Automated Decision-Making which comprises a series of 48 risk and 33 mitigation questions based on systems design, decision type, impacts, and data collection. The AIA is intended to identify risks and assess impacts in a broad range of areas, including the rights, health, and economic well-being of individuals, entities, or communities.

Problem: The risks associated with using AI on VLOPs are not sufficiently understood. As a result, VLOPs are not adequately managing risks which could have profound impacts on the digital public sphere and our democracy.

Obstacle: VLOPs may argue that completing the AIA is costly and that protecting the rights, health, and economic well-being of individuals is a function of the State and not corporations.

Impact: The AIA identifies the level of risk associated with a particular AI or algorithmic system and assigns it an impact level. Impact levels determine required risk mitigation techniques.

Recommendation 2: Transparency

Technical Audit Reporting: VLOPs shall provide information to the Canadian Artificial Intelligence Regulatory Authority (CAIRA) for a technical audit of the technical elements (inputs, outputs, algorithms) of their AI and algorithmic systems (see the "Enforcement and Remedies" section for an explanation of and justification for the establishment of CAIRA).

Problem: AI systems may, intentionally or unintentionally, be trained on biased datasets, resulting in discriminatory outputs or the promotion of hateful content.

Obstacle: VLOPs may claim that their AI systems are proprietary and, therefore, that they should not be mandated to provide details about technical specifications to the government.

Impact: Requiring that VLOPs provide information to CAIRA will allow for greater transparency. The hope is that, by requiring VLOPs to be more transparent, they will be more likely to adopt more robust AI practices.

Recommendation 3: Responsibility-by-Design

Algorithmic Opt-In: VLOPs shall default all user profiles to a non-algorithmically curated feed and instead provide users with the option to opt-in to an algorithmically curated feed.

Problem: Using personal data from users, most VLOPs deploy curation algorithms that tailor users' feeds according to their browsing history, thereby increasing engagement. By creating filter bubbles and echo chambers, algorithmic curation has been found to lead to political polarization and radicalization, thereby undermining democracy.

Obstacle: VLOPs may resist calls for opt-in algorithmic curation because curation practices allow platforms to raise more profit from advertisers, who will pay a premium to place ads in front of a highly engaged audience in a targeted manner.

Impact: Setting non-algorithmically curated feeds as the default will give users more agency over their online experience and how they participate in the digital public sphere. Reducing algorithmic curation will also reduce the proliferation of echo chambers and slow the spread of political polarization across VLOPs.

AI Interaction Disclosure: When AI systems are user-facing, VLOPs must ensure that users are made aware of their interaction with such AI systems through clear labeling practices.

Problem: Currently, VLOPs do not notify users when they are interacting with AI systems. If users are unknowingly exposed to a disproportionate amount of harmful or inaccurate content due to algorithmic curation (rather than a personal choice to consume that content), they may believe they are receiving an accurate and balanced perspective.

Obstacle: VLOPs may prefer not to disclose to their users when they are interacting with AI or algorithmic systems, as this may reduce their credibility.

Impact: Users will become aware of how AI and algorithmic systems impact their ability to make autonomous decisions and form individual opinions, and equip them with the necessary knowledge to challenge this practice by VLOPs.

Right to Justification: If a user's content is removed from a VLOP by an AI-enabled moderation service, that user shall have the right to request justification from the VLOP about how and why their content was removed, including the methods through which the AI-enabled moderation service categorizes content. The VLOP shall respond to users' requests for this justification in a timely manner.

Problem: Though VLOPs often provide this complaint mechanism on a voluntary basis, it is not currently legally necessary. In other words, VLOPs are not required to provide their users with a justification regarding the moderation of their content in a timely manner.

Obstacle: VLOPs may argue that they do not have enough personnel or funds to respond to all justification requests from users.

Impact: This proposal will enhance VLOPs' accountability towards their users and clarify the conditions and circumstances in which VLOPs decide to restrict the right to freedom of expression.

Recommendation 4: Enforcement and Remedies

Regulatory Oversight and Adjudication: CAIRA shall be created as a regulatory and technical body under Innovation, Science and Economic Development Canada (ISED). The Artificial Intelligence Tribunal will be created to administer penalties for contraventions and will be part of the judicial branch to oversee and adjudicate the use of AI systems on VLOPs.

Problem: VLOPs' business practices are largely self-regulated, which may not sufficiently secure the protection of users' fundamental rights and democratic values. In addition, in Canada, there are no oversight or judicial bodies to regulate VLOPs.

Obstacle: VLOPs may argue that establishing a new regulatory and judicial body is a form of unnecessary government overreach in private business.

Impact: The creation of CAIRA and the Artificial Intelligence Tribunal will establish a robust regulatory body to oversee the use of AI systems used by VLOPs; these regulatory bodies will help curb the dissemination of misinformation and disinformation. This will reduce the risk of political polarization and radicalization, fostering a more informed and cohesive democratic society.

Technical Audit Reporting and Public Repository: CAIRA shall conduct an audit of the technical elements (inputs, outputs, algorithm) of AI and algorithmic systems to:

- Assess reliability of AI and algorithmic systems;
- Check AI and algorithmic systems for discriminatory biases;
- Assess other aspects of the function of an algorithmic system

CAIRA shall then prepare and publish a Technical Report in a publicly available repository.

Problem: AI systems may, intentionally or unintentionally, be trained on biased datasets, resulting in discriminatory outputs or the promotion of hateful content.

Obstacle: VLOPs may claim that their AI systems are proprietary and, therefore, that they should not be mandated to provide details about technical specifications to the public.

Impact: The publication of Technical Reports on a publicly available repository will allow for greater transparency. The hope is that, by requiring VLOPs to be more transparent, they will be motivated to adopt more robust AI practices.

Administrative Monetary Penalties: The maximum penalty for all the contraventions by a VLOP taken together is the higher of $15,000,000 and 5% of the organization's gross global revenue in its financial year before the one in which the penalty is imposed.

Problem: In Canada, there are no enforcement or remedial mechanisms in place for the abuse of AI systems in general, including by VLOPs.

Obstacle: Monetary penalties may not necessarily be an effective deterrent against corporations using harmful AI systems (e.g., corporations may see fines as part of running the business).

Impact: Fines would serve as a deterrent against VLOP non-compliance. The funds collected from these fines could also be allocated to organizations dedicated to upholding human rights and democratic values.

Chapter V Conclusion

We currently stand at an inflection point where democracies are being strained by technologies once assumed to be liberatory. But while there is growing recognition of this problem, there remains significant ambiguity and uncertainty about how to appropriately respond to AI and its impact on public discourse. This is because the policy regulation of our public sphere bumps up against norms and ideals of free speech and censorship; open markets and competition policy; innovation and regulation; electoral integrity and political manipulation; and state and private sector governance. In an effort to address these issues and to respond to calls from Canadians for more robust regulation of online hate speech and mis- and dis-information, this policy brief has outlined a series of recommendations that, if taken, will improve the state of democracy in Canada and thus the ability of corporations, including VLOPs, to implement meaningful social responsibility agendas.

Appendices

Appendix 1: Summary of Impact Paper Recommendations

Chapter I – ESG and the Purpose Economy

Recommendation 1: Require Corporations to State their Social Purpose

Target Audience: Federal and Provincial Governments
Actions:
a) Require corporations to state a corporate purpose in their articles of incorporation.
b) Encourage corporations to make binding ESG statements in their by-laws.

Recommendation 2: Reporting for Stakeholder Transparency

Target Audience: Canadian Federal Government: Environment and Climate Change Canada, Health Canada, and the The Health Products and Food Branch, and the United Nations
Actions:
a) Implement a public product rating system, which would rank products on ESG. The government should draw on the NFPA 704 system for identifying chemical substances as an example for how this ranking can be structured.
b) The United Nations should hold an international conference with key global actors. A worldwide metric system quantifying ESG must be created, using an industry-specific approach.

Recommendation 3: Targeted investment by Public and Private Actors

Target Audience: Federal/Provincial/Local Governments, the Business Development Bank of Canada, Investors, Banks, and Asset Managers
Action:
a) Encourage the growth of social purpose corporations through increased targeted investment in the public and private sectors.

Recommendation 4: Supporting ESG and purpose-driven corporations through taxation

Targeting: Federal Government

Action:

a) Amend the Canadian Income Tax Act to develop a special tax status targeted at organisations that meet ESG-related standards throughout their business practices. This special tax status should introduce (1) a sliding scale corporate tax break targeted at SMEs and (2) tax incentives to support corporations implementing ESG-conscious business practices.

Recommendation 5: Integrating Social Purpose within Education and Professional Training

Target Audience: Higher education institutions first, followed by industry/trade associations

Action:

a) Higher-level institutions, starting with business and law schools, should teach current and former students about a purpose-driven economy.

Chapter II – Sustainable Finance

Recommendation 1

(A): *Institutional investors should be given maximum flexibility, incentive and protection in making investment decisions that are climate-compliant and that contribute to meeting the Canadian domestic and international obligations to reduce GHG emissions.*

(B): *Institutional investors should be required by financial regulators to disclose the climate risks in their portfolios at the asset and portfolio levels.*

(C): *The federal government should encourage investment in green technologies and economies by providing appropriate tax incentives.*

Recommendation 2

(A): *Canada should strengthen its Development Finance Institution to catalyze low-carbon growth in the poorest countries.*

(B): *Canada should mobilize Multilateral Development Banks to be more ambitious, risk-tolerant and flexible in providing climate finance to developing countries.*

(C): *Canada should bring together its business and trade promotion organizations behind a comprehensive plan to deploy made-in-Canada climate solutions in developing countries.*

Recommendation 3

(A): *The federal financial regulator (Office of the Superintendent of Financial Institutions) and the Department of Finance should develop uniform, benchmark ESG reporting standards for each sector and asset class to enhance accountability by creating an objective rating standard to assess the environmental risks of each company.*

(B):*The federal and provincial governments should provide financial, training and technical support to small and medium size businesses who may face difficulties in reporting on ESG issues.*

Recommendation 4

(A): *Financial regulators should require rating agencies to fully disclose the methodologies adopted to evaluate corporate ESG performance. They should furthermore explain any revisions they have made to previously assigned ESG ratings.*

(B): *Regulators should set up an independent team/body to oversee the work of ESG rating agencies, investigate whether they have complied with the disclosure requirements., and set up an independent team/body to oversee the work of ESG rating agencies.*

Recommendation 5

(A): *Require establishment of "Chief Sustainability Officers" in Canadian chartered banks to create, implement and report on each bank's sustainability strategy to the federal financial regulator (OSFI).*

(B): *Require establishment of CSOs in shadow-bank institutions and coordinate with provincial jurisdictions to do the same.*

(C): *Pass the Climate-Aligned Finance Act to ensure climate considerations are built into federal government financing and operational activities.*

Recommendation 6:

A New Green New Deal. *The federal government should establish a Ministry of Green Energy Infrastructure (MGEI). The mandate of the MGEI will be to design, finance, build, operate and maintain a green energy infrastructure system (GEIF). The purpose of the GEIF is to provide a publicly funded alternative energy system to fossil-fuel generated electricity. The MGEI will promote and coordinate innovation in financing and investment in emergent green energy technologies.*

Chapter III – Climate Change changes Everything

Recommendation 1: *Environmental Lens - Beyond Net-Zero*

International norm-setting bodies, specifically the Conference of the Parties to United Nations Framework Convention on Climate Change (UNFCCC), must redefine climate-related targets to expand beyond emission and temperature targets to better recognize the interdependence of biodiversity, ecosystems, and social inequities. This can be done completely concretely be done through communication between COPs or task forces.

Recommendation 2: *Economic Lens - Doughnut Overconsume*

The financial sector (banks, corporations and governments) must redefine growth in terms of environmental and social pillars, beyond economic. Value must capture the limitations of finite resources to reduce overconsumption by states, corporations, and affluent individuals.

Recommendation 3: *Technological Lens - A Piece of the Puzzle*

Innovators must prioritize technological solutions that reduce the creation of emissions, not only offset them, and must give due regard to their negative human rights and environmental implications.

Recommendation 4: *Political Lens - UNDRIP in the Green Transition*

Global nations need to participate in implementing the United Nations Declaration on the Rights of Indigenous Peoples (UNDRIP) and must substantively integrate free, prior, and informed consent (FPIC) for all extraction and development projects, especially when related to the green transition.

Recommendation 5: *Justice Lens - Funding Loss & Damage*

A market-share approach must be adopted to fund the Warsaw International Mechanism for Loss and Damage associated with Climate Change Impacts (WIM). Corporations who contribute most to climate change must appropriately compensate those historically and disproportionately impacted.

Chapter IV – Global Value Chains

Recommendation 1: Mandating Visibility

We recommend that regulators should mandate value chain visibility, e.g., adoption of blockchains in order to improve traceability within global value chains.

Recommendation 2: Re-centering Human Value

We recommend that government regulators consult affected foreign actors when drafting legislation and considering the governance of global value chains.

Recommendation 3: Access to effective legal remedies

We recommend that regulators ensure that victims have standing in courts to access effective legal remedies and implement a reversal of the burden of proof.

Recommendation 4: Collaborative Certification Regime

We recommend that regulators and NGOs co-create a certification, tied to financial incentives, recognizing companies that do not use slave labor in their supply chain.

Recommendation 5: Increased policy coherence and ending the siloed approach to addressing modern slavery

We recommend increasing policy coherence by adopting a "whole-of-government approach" and combining the above recommendations into one multi-pronged strategy so as to close existing policy gaps.

Chapter V: Corporations and Democracy in the Age of Digitization & AI

Recommendation 1: Accountability - Algorithmic Impact Assessment (AIA)

VLOPs shall complete the risk assessment mandated under the Canadian Directive on Automated Decision-Making which comprises a series of 48 risk and 33 mitigation questions based on systems design, decision type, impacts, and data collection. The AIA is intended to identify risks and assess impacts in a broad range of areas, including the rights, health, and economic well-being of individuals, entities, or communities.

Recommendation 2: Transparency - Technical Audit Reporting

VLOPs shall provide information to the Canadian Artificial Intelligence Regulatory Authority (CAIRA) for a technical audit of the technical elements (inputs, outputs, algorithms) of their AI and algorithmic systems (see the "Enforcement and Remedies" section for an explanation of and justification for the establishment of CAIRA).

Recommendation 3: Responsibility-by-Design

a) **Algorithmic Opt-In**: VLOPs shall default all user profiles to a non-algorithmically curated feed and instead provide users with the option to opt-in to an algorithmically curated feed.

b) **AI Interaction Disclosure**: When AI systems are user-facing, VLOPs must ensure that users are made aware of their interaction with such AI systems through clear labeling practices.

c) **Right to Justification**: If a user's content is removed from a VLOP by an AI-enabled moderation service, that user shall have the right to request justification from the VLOP about how and why their content was removed, including the methods through which the AI-enabled moderation service categorizes content. The VLOP shall respond to users' requests for this justification in a timely manner.

Recommendation 4: Enforcement and Remedies

a) **Regulatory Oversight and Adjudication:** CAIRA shall be created as a regulatory and technical body under Innovation, Science and Economic Development Canada (ISED). The Artificial Intelligence Tribunal will be created to administer penalties for contraventions and will be part of the judicial branch to oversee and adjudicate the use of AI systems on VLOPs.

b) **Technical Audit Reporting and Public Repository**: CAIRA shall conduct an audit of the technical elements (inputs, outputs, algorithm) of AI and algorithmic systems to:

   i) Assess reliability of AI and algorithmic systems;
   ii) Check AI and algorithmic systems for discriminatory biases;
   iii) Assess other aspects of the function of an algorithmic system.

   CAIRA shall then prepare and publish a Technical Report in a publicly-available repository.

c) **Administrative Monetary Penalties**: The maximum penalty for all the contraventions by a VLOP taken together is the higher of $15,000,000 and 5% of the organization's gross global revenue in its financial year before the one in which the penalty is imposed.

Appendix 2: Chapter V Definitions

Algorithm

One or more processes, set of rules, or methodologies to be followed in calculations, data processing, data mining, pattern recognition, automated reasoning or other problem-solving operations, including those that transform an input into an output.[234]

Artificial intelligence (AI) systems

Technological systems that, autonomously or partly autonomously, process data related to human activities through the use of a generic algorithm, a neural network, machine learning, or another technique in order to generate content or make decisions, recommendations, or predictions.[235]

Content curation

The personalization of content on VLOP users' feeds in order to maximize their attention and engagement.

Content moderation

The removal of content deemed harmful, either through self-regulation or government mandate, from VLOPs.

Disinformation

False information that is deliberately created to mislead people, organizations, and countries.[236]

Misinformation

False information, often shared in good faith, that is not intended to cause harm.[237]

Platforms

Host, organize, and circulate users' shared content or social interactions, without having produced (the bulk of) that content.[238]

Political polarization

Differing from institutional distrust and democratic dissatisfaction, a phenomenon whereby policy preferences across groups of people become more distant over time and partisan groups become more hostile toward one another.[239]

Political radicalization

Anti-social attitudes and perceptions often caused by the consumption of ideological content.

Platform

A website with a core function to distribute one person's content to another.

Very Large Online Platform (VLOP)

Online platforms with a user base comprising more than 10% of any given population. In Canada, a VLOP must have at least 3.8 million users.[240]

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