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Can ESG Culture Be Acquired? Essays on Corporate Culture, Governance, and Sustainability Transformation

By

Silvia Regina Fregoni

A dissertation submitted in partial satisfaction of the
requirements for the degree of
Doctor of the Science of Law – Juris Scientiae Doctor (J.S.D.)
in the
Graduate Division
of the
University of California, Berkeley

Committee in charge:

Professor Adam Badawi, Chair

Professor Stavros Gadinis

Professor Frank Partnoy

Professor Steven Davidoff Solomon

Summer 2025

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Abstract

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By

Silvia Fregoni

Doctor of the Science of Law – Juris Scientiae Doctor (J.S.D.)

University of California, Berkeley

Professor Adam Badawi, Chair

This dissertation investigates how corporate sustainability culture emerges, evolves, and can be reshaped within firms. It integrates three papers that examine cultural change through theoretical, legal, and empirical lenses. The first paper develops a conceptual framework for understanding the drivers of corporate culture change, presenting a taxonomy of internal and external catalysts—including leadership transitions, regulatory pressures, and strategic transactions such as mergers and acquisitions (M&A)—and outlines a research agenda for future interdisciplinary inquiry. The second paper analyzes how emerging global regulations and voluntary initiatives are reshaping corporate governance structures, including board oversight, disclosure practices, and accountability mechanisms. It argues that a structural shift toward "corporate sustainability governance" is underway and is unlikely to be easily reversed, even in the face of ESG backlash. The third paper empirically tests whether ESG culture can be transferred through M&A. The findings indicate that acquirers frequently enhance their ESG culture post-transaction by adopting practices from stronger ESG targets, particularly when the acquirer is substantially larger. However, these cultural improvements are not immediately reflected in market valuations. Together, the papers offer a multidimensional analysis of how sustainability values spread within corporations.

To Ricardo, Bruno, and Helena — for your infinite love, patience, and unwavering support.

To my parents, Geni and Atilio, and to my sister, Ana Paula — for encouraging me from my earliest days and believing in me every step of the way.

And to my beloved brother, Junior, who left us far too soon during the final year of this journey. I will love you forever! *E até algum dia!*

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Preface

This dissertation argues that corporations are key actors in shaping not only markets but also the social and environmental conditions in which they operate. On the one hand, they are often viewed primarily as engines of economic growth, judged by their financial performance. On the other hand, less attention is paid to how corporate culture, governance, and strategy influence their role in addressing—or exacerbating—global sustainability challenges. From my years as a journalist covering business, finance, and capital markets, I developed a lasting interest in how law, market forces, and organizational behavior interact in this space. To explore these questions, I present three studies, summarized as follows.

The first paper, *Beyond Tone at the Top: A Taxonomy of What Drives Corporate Culture Change*, examines the main catalysts of corporate culture transformation, drawing on literature from psychology, sociology, management, economics, and law. Corporate culture plays a vital role in how businesses function, influencing everything from strategic decisions and employee engagement to regulatory compliance and a firm's ability to adapt to uncertainty, consequently impacting financial performance. While scholars have extensively examined culture's effects on business outcomes, less attention has been paid to how culture changes over time, and whether it can be deliberately reshaped. This paper addresses this gap by offering a taxonomy of cultural change catalysts, categorizing them into internal and external forces. It also distinguishes between slow-moving, evolutionary processes and sudden, disruptive shocks. In doing so, it builds on existing scholarship while advancing a conceptual framework for understanding the dynamics of cultural transformation. Finally, the paper looks ahead. It lays out a research agenda calling for more empirical work to test theories of cultural change and advocates the use of emerging tools, such as large language models, to analyze unstructured data from sustainability reports, employee reviews, executive speeches, and social media. It also highlights promising theoretical directions for future exploration, such as mutual constitution, which emphasizes the reciprocal influence between individual psychology and organizational culture. The goal is to help scholars, regulators, and corporate leaders better understand what really drives cultural change, and how to study it in meaningful, practical ways.

The second paper, *Corporate Sustainability Governance*, argues that a new governance regime is taking shape within modern corporations, without any formal changes to corporate law and despite mounting political backlash. In recent years, companies have faced intensifying pressure to address climate risk, human rights, and other sustainability challenges as core elements of their operations. These demands have reshaped what it means to govern a corporation: beyond financial oversight, directors and executives are now expected to supervise environmental and social risks as well. This evolution is giving rise to what I term "corporate sustainability governance," a governance regime that integrates environmental and social concerns into the core architecture of corporate oversight, internal controls and processes, risk management, and possible decision-making. This paper builds on recent scholarship that identifies the rise of corporate climate governance, driven by regulation, but expands this view in two key ways. First, it argues that the change goes beyond climate and involves a wider range of issues, including human rights, labor standards, and supply chain due diligence. Second, it demonstrates that this transformation is not solely regulation-driven; rather, it emerges from a complex interplay between regulatory mandates and voluntary corporate initiatives and commitments. Although the underlying framework of American corporate law remains unchanged, many U.S. corporations have already shifted aspects of their governance toward stakeholder considerations—sometimes robustly, sometimes superficially—mirroring the variation found in traditional corporate governance practices. The institutionalization of these new governance mechanisms, along with global developments in this area and peers' competition, means that they are unlikely to be easily and readily dismantled, even amid political backlash or the potential reversal of specific regulations. By tracing the institutionalization of sustainability through both public and private channels, this paper reconceptualizes corporate governance in modern times and offers insights that have implications for ongoing debates on climate and social disclosure, corporate purpose, the evolving role of the board, and managerial incentives.

The third paper, *Can ESG Culture Be Acquired? The Impact of M&A on Sustainability Practices and Market Perceptions*, empirically tests one of the potential drivers of cultural change identified in the first paper: mergers and acquisitions as a mechanism for "transferring" ESG culture from one firm to another. Despite the recent political and ideological backlash, environmental and social concerns continue to lead the debates across boardrooms, policymaking,

and scholars. One key question persists: how can ESG culture be shaped—and reshaped—within firms over time? This paper examines that question in the context of mergers and acquisitions (M&A), major transformative events that can impact corporate governance and leadership, in addition to market positioning and performance. The findings show that companies can, in effect, "acquire" ESG culture by buying targets with stronger ESG profiles. In such case, acquirers' ESG improvement is significant and consistent over time, supporting the theory that firms can learn practices and absorb knowledge from the firms they purchase. However, these gains are not immediately rewarded by investors. While abnormal stock returns tend to be directionally positive following such deals, they are not statistically significant up to one year after the announcement, consistent with the theory that markets often struggle to incorporate the value of intangibles into prices in the short- and medium-term. This paper contributes to both the ESG and the M&A literature by examining a novel intersection: the transmission of sustainability culture through acquisition. It also offers policy-relevant insights for regulators, managers, and stakeholders interested in how corporate values can evolve in response to structural change.

As the summaries indicate, the research that led to this dissertation approaches the interaction between law, markets, and corporate behavior from a comparative perspective, using theoretical, legal, and empirical lenses. It draws on corporate governance theory, corporate finance, and regulatory analysis, while incorporating evidence from market data and real-world corporate practice. I hope these findings will inform and inspire scholars, practitioners, and policymakers navigating this evolving landscape.

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I also thank the staff of Berkeley Law, especially those involved in administering the J.S.D. program, for their invaluable assistance throughout my doctoral studies. My gratitude extends to all the professors and instructors whose lectures, feedback, and conversations enriched my thinking and informed my work.

This work was made possible through the generous support of the Robbins J.S.D. Fellowship, my primary sponsor. I was also honored to be a Berkeley Empirical Legal Studies (BELS) Fellow and a Miller–American Society of International Law (ASIL) Fellow, experiences that provided valuable resources and opportunities for my learning and progress. I am equally grateful to the Berkeley Center for Law and Business (BCLB), where I have worked over the past three years, and to its team for the infinite opportunities to learn and grow in an intellectually vibrant environment.

My heartfelt thanks go to the friends whose companionship sustained me through this journey—Elizabeth Alvaro, Luis Otavio Barroso da Graça, Mahwish Moazzam, and Sharaban Tahura Zaman, among many others—whose friendship, solidarity, and laughter made the challenges lighter and the milestones more joyful.

Above all, I owe my deepest gratitude to my family. To my husband, Ricardo, for his patience, understanding, and steadfast belief in me. To my children, Bruno and Helena, for filling my life with joy and perspective, and for reminding me daily of what truly matters. To my parents, sister, and extended family, for their unwavering encouragement and love across the miles. This accomplishment is as much theirs as it is mine.

Any remaining errors or shortcomings in this work are mine alone.

Part I

Beyond Tone at the Top: A Taxonomy of What Drives Corporate Culture Change

1. Introduction

"My main job today: I work hard at helping to maintain the culture," Jeff Bezos once stated at a Business Insider conference.[1] This focus on culture is not incidental at Amazon, a company often described as high-performance, customer-obsessed, and data-driven,[2] yet also intense and demanding.[3] On the other end of the spectrum, Costco operates with a very different model, emphasizing employee loyalty, operational frugality, and long-term stability,[4] but its co-founder Jim Sinegal was equally resolute in affirming the importance of culture: "Culture is not the most important thing in the world. It is the only thing."[5] These contrasting examples reflect the growing consensus in the business world that corporate culture is no longer a soft, peripheral issue, but a strategic element. As the shared set of values and norms that shape how employees work and

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[1] *See* Jodi Kantor & David Streitfeld, *Inside Amazon: Wrestling Big Ideas in a Bruising Workplace*, N.Y. TIMES (Aug. 15, 2015), https://www.nytimes.com/2015/08/16/technology/inside-amazon-wrestling-big-ideas-in-a-bruising-workplace.html (last visited May 5, 2025).

[2] *See, e.g.,* Gustavo Razzetti, *How Amazon Built a Culture of Innovation by Working Backwards, Fearless Culture*, Fearless Culture Design Blog (Sept. 8, 2021), https://fearlessculture.design/blog-posts/how-amazon-built-a-culture-of-innovation-by-working-backwards (last visited May 5, 2025).

[3] *See, e.g.,* Olivia Solon, *Amazon's Brutal Work Culture Isn't the Exception – It's the Future,* GUARDIAN (Aug. 22, 2015), https://www.theguardian.com/commentisfree/2015/aug/22/amazon-brutal-work-culture (last visited May 5, 2025).

[4] *See, e.g.,* Charles Fishman, *The Costco Craze: Inside the Warehouse Giant's Success*, CNN MONEY (Oct. 27, 2011), https://money.cnn.com/2011/10/26/news/companies/costco_wholesale_secret_pricing.fortune/index.htm (describing Costco's operational model built on frugality, limited product selection, and strong employee retention practices).

[5] *See* Brendan Byrnes, *Costco Co-Founder: "Culture Is Not the Most Important Thing -- It's the Only Thing"*, THE MOTLEY FOOL (Aug. 21, 2013), https://www.fool.com/investing/general/2013/08/21/costco-leader-culture-is-not-the-most-important-th.aspx (last visited Apr. 5, 2025).

innovate, culture defines not only a company's internal cohesion but also how it navigates public scrutiny and long-term performance.[6]

Corporate culture has also become central to some of the most contentious debates in corporate law and governance today. The growing polarization between proponents of stakeholder capitalism and critics of so-called "woke capitalism"[7] has brought questions of purpose, identity, and values into the legal and economic spotlight. At the heart of these debates lies a fundamental concern: How are corporate values defined, communicated, and operationalized, and by whom? Corporate culture plays a crucial role in answering these questions. It provides the systems and shared understandings through which organizational purpose and values are interpreted and translated into action.[8] Culture guides behavior in the absence of rules, aligns employees with strategic goals, and enables organizations to adapt to uncertainty.[9]

A good corporate culture, rooted in integrity, has been associated with stronger firm performance,[10] higher employee motivation,[11] and organizational resilience.[12] Studies show that when internal norms align with stated values, companies are more likely to earn stakeholder trust

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[6] *See generally* JAMES HESKETT, THE CULTURE CYCLE: HOW TO SHAPE THE UN*SEEN* FORCE THAT TRANSFORMS PERFORMANCE (FT Press 2011).

[7] *See, e.g.,* Jack Pitcher, *BlackRock's 'Woke' Era Is Over,* WALL ST. J. (Mar. 2, 2025), https://www.wsj.com/business/blackrocks-woke-era-is-over-ebdbd6e7; *Stephen Foley, Banks' Climate Climbdowns Show Limits of Stakeholder Capitalism*, FIN. TIMES (Feb. 4, 2024), https://www.ft.com/content/aa5f901f-bd66-473a-a4e6-19ad2a2d4bed.

[8] *See* Charles A. O'Reilly III, Jennifer A. Chatman & David F. Caldwell, *People and Organizational Culture: A Profile Comparison Approach to Assessing Person-Organization Fit*, 34 ACAD. MGMT. J. 487, 488–90 (1991) (describing culture as a shared interpretive framework that guides individual behavior and aligns employees with organizational values).

[9] *See, e.g.,* JAMES L. HESKETT & JOHN P. KOTTER, CORPORATE CULTURE AND PERFORMANCE 25–26 (FT Press 2011) (discussing how culture supports decision-making in uncertain environments and reinforces strategic alignment).

[10] *See, e.g.,* Luigi Guiso, Paola Sapienza & Luigi Zingales, *The Value of Corporate Culture*, 117 J. FIN. ECON. 60 (2015), https://doi.org/10.1016/j.jfineco.2014.05.010 (finding that firms with strong cultural integrity outperform peers and enjoy higher profitability and stock returns)

[11] *See, e.g.,* John R. Graham, Campbell R. Harvey, Jillian Popadak & Shivaram Rajgopal, *Corporate Culture: Evidence from the Field*, 145 J. FIN. ECON. 352, 352–84 (2022) (showing that culture significantly affects employee motivation and effort, based on a large survey of executives).

[12] *See, e.g.,* Jennifer A. Chatman, David F. Caldwell, Charles A. O'Reilly III & Bernadette Doerr, *Parsing Organizational Culture: How the Norm for Adaptability Influences the Relationship Between Culture Consensus and Financial Performance in High-Technology Firms*, 35 J. ORG. BEHAV. 785, 785–808 (2014) (demonstrating that adaptability as a cultural trait contributes to long-term firm performance, especially under change or uncertainty).

and avoid governance failures.[13] Conversely, bad corporate culture has been linked to corporate scandals,[14] ethical breakdowns,[15] and reputational damage.[16] In many of the most high-profile corporate failures of the past two decades, culture played an enabling role,[17] tolerating misconduct, discouraging accountability, and prioritizing short-term results over long-term responsibility.[18] The gap between what companies *say* and what they *do* can erode trust, increase legal and reputational risk, and lead to employee disengagement.[19] These challenges highlight the urgent need not only to understand what corporate culture *is*, but also how it *changes*, and under what conditions that change becomes real rather than rhetorical.

Importantly, corporations are unique and crucial institutions in modern society, not only due to their legal structure and great economic impact but also because of their internal complexity.[20] Companies are not simply machines that turn inputs into outputs. They operate

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[13] *See* Heskett & Kotter, *supra* note 9.

[14] *See, e.g.,* Ronald R. Sims & Johannes Brinkmann, *Enron Ethics (Or: Culture Matters More Than Codes)*, 45 J. BUS. ETHICS 243, 243–56 (2003) (exploring how Enron's internal culture enabled its downfall beyond formal ethics programs).

[15] *Id.*

[16] *See, e.g.,* Robert G. Eccles, Ioannis Ioannou & George Serafeim, *The Impact of Corporate Sustainability on Organizational Processes and Performance*, 60 MGMT. SCI. 2835, 2835–57 (2014) (showing that firms with stronger sustainability-oriented governance frameworks tend to outperform peers and reduce reputational and stakeholder risk).

[17] *See* Xiaoding Liu, *Corruption Culture and Corporate Misconduct*, 122 J. Fin. Econ. 307, 307–27 (2016) (finding that firms with high corruption culture are more likely to engage in earnings management, accounting fraud, option backdating, and opportunistic insider trading).

[18] *See* Tom W. Reader & Alex Gillespie, *Target Pressure and Corporate Scandals: A Natural Language Processing Investigation of How Organizational Culture Underlies Institutional Failures*, 97 J. OCCUPATIONAL & ORG. PSYCHOL. 855 (2024), https://doi.org/10.1080/1359432X.2024.2398181 (finding that organizational cultures emphasizing unrealistic performance targets can foster misconduct and risk-taking, contributing to corporate scandals).

[19] *See* Q. Miao & J. Zhou, *Corporate Hypocrisy and Counterproductive Work Behavior: A Moderated Mediation Model of Organizational Identification and Perceived Importance of CSR*, 12 SUSTAINABILITY 1847 (2020), https://doi.org/10.3390/su12051847 (finding that perceptions of corporate hypocrisy are associated with increased counterproductive behavior by employees); Hongdan Zhao, Jing Xu, Yuanhua Chen & Wenyuan Sun, *The Employee Attributions of Corporate Hypocrisy in Corporate Social Responsibility: An Exploratory Study Based on Grounded Theory*, 10 SAGE OPEN 1, 1–22 (Apr. 2020), https://doi.org/10.1177/2158244020924427 (exploring how employees attribute corporate hypocrisy in CSR).

[20] *See, e.g.,* LYNN A. STOUT, THE SHAREHOLDER VALUE MYTH: HOW PUTTING SHAREHOLDERS FIRST HARMS INVESTORS, CORPORATIONS, AND THE PUBLIC 26–30 (Berrett-Koehler 2012) (arguing that corporations are complex, durable institutions with distinct legal and organizational features that serve broader societal purposes beyond profit maximization).

through norms and routines that determine how decisions are made and how work gets done. These internal cultures do not stay within firm boundaries. They influence how companies treat their workers, interact with the environment, allocate capital, and engage with communities, for example.[21] As such, corporate behavior, rooted in culture, has wide-reaching implications for social welfare and even democratic accountability.[22] In this sense, the internal culture of firms is not only a matter of organizational performance, but a key factor in how corporations exercise public power.[23]

A growing body of research shows that many of the differences we see between companies, such as how well they perform and how innovative or resilient they are, cannot be explained just by size, industry, or resources.[24] Instead, a major driver of these differences is culture: the internal beliefs and behaviors that guide decision-making and collaboration.[25] That is why corporate culture deserves a central place in organizational analysis, not just as a behavioral lens, but as a driver of performance and strategic direction.

Understanding corporate culture is especially important in light of growing critiques of some long-standing assumptions in economics and law. For decades, the dominant view, based on property rights[26] and agency theory[27], has focused on the idea that managers are self-interested actors who need to be tightly monitored. While that model has illuminated key governance problems, it often overlooks the role of culture. Trust, shared purpose, and social norms can shape

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[21] *See* Stavros Gadinis, *Social Business Judgment* (June 6, 2025) (forthcoming in *Bus. Law.*), https://ssrn.com/abstract=5284487.

[22] *Id.*

[23] *See* Ronen Shamir, *The Age of Responsibilization: On Market-Embedded Morality*, 37 ECON. & SOC'Y 1, 3–7 (2008) (explaining how internal corporate norms and self-regulation increasingly function as mechanisms of public governance and norm-setting in neoliberal economies).

[24] *See, e.g.,* Graham et al., *supra* note 11 (reporting results from a large-scale survey and interviews with executives, finding that corporate culture is a key driver of firm value, and unethical behavior is often a symptom of cultural failure).

[25] *Id.*

[26] *See* Gregory K. Dow, GOVERNING THE FIRM: WORKERS' CONTROL IN THEORY AND PRACTICE (Cambridge University Press 2003) (arguing that property-rights theories fail to explain why capital owners rather than workers control firms and overlook normative governance concerns).

[27] *See* Margaret M. Blair & Lynn A. Stout, *A Team Production Theory of Corporate Law*, 85 VA. L. REV. 247, 247–328 (1999) (arguing that corporations should be viewed as team production processes requiring trust and internal coordination, rather than mere nexuses of contracts between shareholders and managers).

behavior just as formal contracts or incentives do. A cultural perspective brings these elements back into focus. It gives space for deeper questions, such as whether there is a "right" kind of culture for every firm, whether culture can be intentionally changed, and which tools actually help make those changes stick.

Corporate culture has been studied across several disciplines—psychology, sociology, management, economics, and law—but many of these studies focus primarily on the effects of culture on firm outcomes.[28] Through a multidisciplinary review of the literature, this paper finds that comparatively less attention has been paid to the drivers of cultural change. This paper addresses this gap by offering a taxonomy of the main theoretical drivers of cultural change. It argues that corporate culture is shaped by internal forces (such as the interaction of individuals, incentives, and organizational structures) and external forces (including regulatory shifts, political change, economic transformations, and broader societal trends).[29] It also distinguishes between slow-moving processes and sudden shocks. Understanding this system, and the conditions under which it evolves, is essential for scholars, regulators, investors, and corporate leaders alike.

By clarifying what corporate culture is—and what it is not—this paper contributes to ongoing scholarly debates that often conflate culture with values, ethics, or compliance. It also offers a framework for empirical analysis. Finally, the paper outlines a research agenda. It encourages empirical work to test theories of cultural change and calls for the use of new tools, such as large language models and machine learning, to analyze culture through unstructured data, including sustainability reports, employee reviews, CEO speeches, and social media posts. It also highlights conceptual frameworks worth exploring, such as the theory of mutual constitution, which emphasizes the reciprocal influence between individual psychology and organizational culture, and suggests new questions for interdisciplinary study.

This paper builds on recent efforts to integrate corporate culture into economic analysis. In particular, Grennan and Li outline how people, systems, and events shape corporate culture and

[28] *See infra* Part 2.

[29] *See infra* Part 4.

emphasize the need for further empirical research in this area.[30] This essay complements and extends their framework by offering a conceptual taxonomy of cultural change catalysts and situating them within broader legal, governance, and societal contexts. It also contributes to a normative dimension by asking not only how culture evolves, but why it matters, particularly in an environment where stakeholder expectations, regulatory mandates, and political pressures increasingly influence the internal dynamics of the firms.

The remainder of the paper proceeds as follows. Part 2 shows the evolution of corporate culture as a field of study. Part 3 defines corporate culture and clarifies its conceptual boundaries, distinguishing it from adjacent constructs such as compliance systems and governance mechanisms. Part 4 presents a taxonomy of catalysts of cultural change in organizations. Part 5 outlines conceptual and methodological directions for future research, while Part 6 concludes.

2. The Evolution of Corporate Culture as a Field of Study

This paper is ultimately concerned with understanding what drives corporate culture change. To get there, however, it is essential to trace how this sometimes nebulous concept of corporate culture emerged and evolved across academic disciplines. The way culture is defined, measured, and understood has shaped how scholars think about whether and how it can change. This chapter explores the intellectual roots of corporate culture as a field of study, highlighting how different disciplines have contributed to its development and how those contributions have shaped theories about cultural stability and transformation.

From early theories of management and organizational behavior to more recent work in sociology, economics, and law, the study of corporate culture has gradually moved from the margins to the center of debates about firm governance and performance. As this chapter demonstrates, early scholarship often treated culture as a background condition rather than a driver of organizational performance. Only later did researchers begin to seriously examine culture as a dynamic force: one that evolves in response to leadership, governance structures, regulation, and

[30] *See* Jillian Grennan & Kai Li, *Corporate Culture: A Review and Directions for Future Research* (Apr. 28, 2022) (unpublished manuscript), available at SSRN, https://ssrn.com/abstract=4095565 (last visited Aug. 6, 2025).

broader societal pressures. By tracing this evolution, the chapter provides the groundwork for the paper's core argument: that culture is not static, but shaped by identifiable internal and external catalysts, which this paper organizes into a conceptual taxonomy.

2.1. The Early Stages of Culture: Historical and Theoretical Foundations

Corporate culture, now widely recognized as a fundamental component of companies' life, emerged as a distinct field of study in the mid-20th century. However, some of its elements began to be identified much earlier,[31] not through academic theorizing, but through the practical efforts of business leaders trying to improve firms' efficiency. These empirical insights gradually informed broader theories of management and organizational behavior.

For example, engineer Frederick Taylor introduced "Scientific Management" as a fundamental concept during the early 1900s to boost productivity and economic efficiency.[32] His approach to management involved breaking tasks into smaller steps, standardizing them, measuring, and increasing employee supervision.[33] According to him, there was a best way of doing things, and this optimal management system required "initiative and incentive": management would provide clear guidance and incentives, while workers would put in their best efforts.[34] Although Taylor was primarily interested in efficiency, he implicitly recognized the need to influence worker behavior, a point that would become central to later theories of organizational culture.[35]

Also at the beginning of that century, engineer Henri Fayol created the so-called 14 Principles of Management, a set of guidelines for managers to improve organizational efficiency and effectiveness. The principles included work division and disciplinary measures, along with

[31] *See* Calvin Morrill, *Culture and Organization Theory*, 619 ANNALS AM. ACAD. POL. & SOC. SCI. 15, 15-21 (2008), for a comccprehensive overview of the early studies on culture and organizational theory.

[32] *See generally* FREDERICK W. TAYLOR, THE PRINCIPLES OF SCIENTIFIC MANAGEMENT 5-10 (Harper & Bros. 1911).

[33] *Id.*

[34] *Id.* at 36.

[35] *Id.*

single command structures and employee interest subordination to organizational goals, for example. The concept of "esprit de corps" received special attention from Fayol because it represented the need to build teamwork, unity, and employee belonging, which matches the modern understanding of company culture.[36] However, like his contemporary Taylor, Fayol did not develop this idea into a theory of culture. Additionally, while both emphasized hierarchy and managerial control, their focus differed: Taylor concentrated on optimizing labor processes at the shop floor level, whereas Fayol developed principles for managing entire organizations from the executive level.[37] Their approaches were distinct, yet both contributed to the foundational theories of classical management.

A maybe more explicit influence on the cultural thinking came from Chester Barnard, a business executive who viewed organizations as cooperative systems. In his influential book, *The Functions of the Executive* (1938), Barnard argued that employee behavior is shaped not just by formal authority but also by informal social structures in the workplace.[38] He presented a "theory of cooperation and organization" that emphasized the importance of communication, leadership, and the willingness of employees to keep corporate cohesion.[39] Barnard's ideas opened the door to a deeper understanding of workplace norms and informal structures, laying the groundwork for the Human Relations Movement that would emerge later in the 1930s.[40]

The production model developed by Toyota Motor Corporation offers another powerful example of practice influencing theory. In postwar Japan, the company created what became the Toyota Production System: a management philosophy centered on lean production, continuous

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[36] *See* Henri Fayol, *General Principles of Management*, in ORGANIZATION THEORY: SELECTED READINGS 181, 181–202 (D.S. Pugh ed., 2d ed. 1984) (Penguin Books) (originally published 1919).

[37] *See* Richard Parker & Andrew Ritson, *Revisiting Fayol: Anticipating Contemporary Management*, 16 Brit. J. Mgmt. 175, 175–94 (2005), https://doi.org/10.1111/j.1467-8551.2005.00453.x.

[38] *See generally* CHESTER I. BARNARD, THE FUNCTIONS OF THE EXECUTIVE (Harvard Univ. Press 1938).

[39] *Id. See also* Jeffrey J. McNally, *The Functions of the Executive [review of the book by C. Barnard*], 17 ACAD. MGMT. LEARNING & EDUC. 1 (2018), https://www.researchgate.net/publication/336288518_The_functions_of_the_executive_Review_of_the_book_by_C_Barnard (examining the enduring influence of Barnard's work and reflecting on its relevance to contemporary management theories).

[40] *See* Morrill, *supra* note 31, at 19-21.

improvement (*kaizen*), and respect for workers at all levels of the firm.[41] Toyota's system represented a break from earlier models, especially Taylorism. While Taylor highlighted top-down control, with close employee supervision, Toyota relied more on worker initiative, collaborative problem-solving, and routines that fostered a sense of collective responsibility.[42] Although it was not framed as "corporate culture" at that time, the system clearly reflected cultural elements, such as shared rituals, values, and expectations, in addition to a commitment to employee empowerment. Over time, Toyota's practices became a reference point for scholars and executives interested in how internal culture and values can enhance organizational performance.

While Taylor, Fayol, Barnard and Toyota's models represented critical practical insights to the study of organizational behavior, in the 1930s a new academic perspective emerged in the United States with the rise of the Human Relations School, which expanded Barnard's initial work on informal norms and cooperation. The movement emerged at Harvard Business School through psychologist Elton Mayo and other scholars who demonstrated that worker productivity depended on both material workplace conditions and social connections (e.g., lighting and sound) and workplace attitudes and relationships.[43] The Hawthorne Studies conducted at AT&T's Western Electric plant by researchers provided experimental evidence that employee performance improved when managers paid attention and employees interacted socially, thus contradicting the rigid rationalist organizational view.[44] The experiments resulted in the discovery of the "Hawthorne Effect", which explains how workers produce more when they feel observed.[45] The research discoveries shifted organizational studies toward the examination of organizational norms, informal networks, and the psychological dimensions of work.

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[41] *See* JEFFREY K. LIKER, THE TOYOTA WAY: 14 MANAGEMENT PRINCIPLES FROM THE WORLD'S GREATEST MANUFACTURER (McGraw-Hill 2004) (describing the development of the Toyota Production System and its emphasis on lean manufacturing, continuous improvement (kaizen), and respect for people).

[42] *See* JAMES P. WOMACK, DANIEL T. JONES & DANIEL ROOS, THE MACHINE THAT CHANGED THE WORLD (Rawson Associates 1990) (tracing the origins and global influence of lean production and the Toyota Production System following World War II).

[43] *See* ELTON MAYO, THE HUMAN PROBLEMS OF AN INDUSTRIAL CIVILIZATION 55-73 (Harvard Univ. Press 1933).

[44] *See* FRITZ ROETHLISBERGER & WILLIAM DICKSON, MANAGEMENT AND THE WORKER 79-83 (Harvard Univ. Press 1939).

[45] *See* Arthur W. Kornhauser**,** *Review of* Elton Mayo, *The Human Problems of an Industrial Civilization*, 172 Annals Am. Acad. Pol. & Soc. Sci**.** 171 (1934), https://doi.org/10.1177/000271623417200135.

However, during the 1930s and 1940s, organizational culture was still framed instrumentally as a factor to increase efficiency and productivity. It was just around the 1950s and 1960s that scholars went beyond this perspective, investigating how organizational culture functioned as an independent force and how it influenced both workplace behavior and institutional stability.[46]

2.2. When the Concept of Corporate Culture Starts to Take Shape

Influenced by these early theories, psychologists and sociologists were the scholars who further transformed corporate culture into a recognized field of study. They moved away from a purely "mechanistic view of management"[47] toward an understanding of organizations as more social systems. While psychology researchers offered micro-level insights (group dynamics, motivation, leadership), sociology scholars contributed with macro-level perspectives (institutionalization, power, norms, and meaning-making in organizations).

Economic developments of that time contributed to the increasing focus on corporate behavior. The economic boom after World War II produced huge, bureaucratic businesses, often operating in different industries and regions, that required new management concepts, beyond the search for efficiency.[48] The theories at that time, such as the ones derived from Taylor and Fayol's work,[49] were no longer sufficient to deal with the dynamics of more complex organizations. This led academics in the 1950s and 1960s to begin considering different concepts, such as workplace behavior and corporate identity. The development of large organizations then helped to highlight the need to understand organizational culture as a factor in business success.

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[46] *See* PHILIP SELZNICK, LEADERSHIP IN ADMINISTRATION: A SOCIOLOGICAL INTERPRETATION 138–40 (Row, Peterson 1957).

[47] *See* AGILE APPLIED, *Mechanistic vs. Humanistic Views of Organizations*, https://agileapplied.com/2016/11/18/two-opposing-views-organizations/ (last visited Mar. 18, 2025).

[48] *See* ALFRED D. CHANDLER JR., STRATEGY AND STRUCTURE: CHAPTERS IN THE HISTORY OF THE AMERICAN INDUSTRIAL ENTERPRISE (MIT Press 1962) (exploring how large American corporations adapted their organizational structures in response to growth and diversification, requiring new management strategies).

[49] *See* Taylor, *supra* note 32.

The larger social and political context also affected organizational theory development. During the Cold War, concerns about ideological stability and national security extended beyond the geopolitical arena to domestic institutions, including corporations.[50] Governments, especially in Western democracies, viewed cohesive and stable organizations as vital to maintaining social order and economic strength in contrast to the perceived chaos of communism. As a result, a great part of the research at that time was supported or driven by a goal to achieve stability in organizations.[51] That would mean not merely increasing productivity, but preventing labor unrest, reducing turnover, and ensuring loyalty to corporate and national values. Simultaneously, society saw the rise of civil rights and labor union movements around the 1960s, which challenged the traditional corporate hierarchies.[52] These societal pressures pushed organizations to rethink their internal arrangements, including power relations and cultural values, setting the stage for a more participative and human-centered style of management.[53]

In this context, academic interest in corporate culture gained traction in both psychology and sociology. Social psychologists were interested in understanding how people adapt to firms' environments and how group dynamics influence attitudes and behavior.[54] In turn, industrial-organizational psychologists wanted to optimize workplace efficiency and leadership effectiveness, while keeping worker well-being.[55] In sociology, the study of corporate culture

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[50] *See* Kenneth N. Waltz, *Structural Realism After the Cold War*, 25 INT'L SEC. 5 (2000) (arguing that post–Cold War institutional stability shaped scholarly priorities in organizational and political theory).

[51] *See* Michael C. Desch, *War and Strong States, Peace and Weak States?*, 50 INT'L ORG. 237 (1996) (examining how security threats during the Cold War strengthened state and institutional capacities, influencing organizational structures).

[52] *See* Robert Korstad & Nelson Lichtenstein, *Opportunities Found and Lost: Labor, Radicals, and the Early Civil Rights Movement*, 75 J. AM. HIST. 792 (1988), https://doi.org/10.2307/1901530 (exploring how civil rights and labor activism prompted reevaluation of workplace hierarchies and corporate norms).

[53] *See* Larry W. Isaac, Steve McDonald & Greg Lukasik, *Takin' It from the Streets: How the Sixties Mass Movement Revitalized Unionization*, 112 AM. J. SOC. 46, 46–96 (2006) (analyzing how social movements of the 1960s influenced the adoption of participatory approaches to corporate management).

[54] *See* Laura L. Koppes, *History of Industrial Organizational Psychology*, in OXFORD RESEARCH ENCYCLOPEDIA OF PSYCHOLOGY (2017), https://oxfordre.com/psychology/view/10.1093/acrefore/9780190236557.001.0001/acrefore-9780190236557-e-39 (last visited Aug. 6, 2025) (providing an overview of the origins and development of industrial-organizational psychology and its role in shaping corporate culture studies).); LUDY T. BENJAMIN JR., A BRIEF HISTORY OF MODERN PSYCHOLOGY (Blackwell 2007) (tracing historical developments of industrial–organizational psychology).

[55] *Id.*

began within organizational sociology, a subfield that examines how social structures, institutional norms, and informal practices operate inside and across firms.[56] Specifically, these sociologists wanted to analyze how culture reinforces authority, mediates power relations, and contributes to corporate stability or change.[57]

One of the most influential authors was Kurt Lewin,[58] whose work on group dynamics and organizational change laid the foundation for understanding how corporate culture evolves.[59] Lewin's Field Theory established that behavior is a function of the individuals and their environment, highlighting the role of social structures in shaping workplace conduct.[60] Then, he created a change management model with three steps: unfreezing (identifying the need for change), changing (implementing the change), and refreezing (stabilizing the new state). The model, using the analogy of changing the shape of a block of ice, became key for understanding and managing corporate culture, particularly during periods of change.[61]

Likewise, Abraham Maslow's hierarchy of needs helped shift management focus toward worker motivation and satisfaction, further reinforcing the psychological dimensions of corporate culture.[62] He offered a new way to think about what motivates employees: not just in terms of pay or job security, but also through deeper needs like belonging, recognition, and self-fulfillment.[63] In sociology, Robert Jackall developed a critical sociological perspective on corporate culture,

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[56] *See* LEOPOLD RINGEL, *Organizational Sociology and Organization Studies: Past, Present, and Futur*e, in SOCIOLOGICAL THINKING IN CONTEMPORARY ORGANIZATIONAL SCHOLARSHIP (Stewart Clegg, Michael Grothe-Hammer & Kathia Serrano Velarde eds., Emerald Pub. Ltd. 2024), https://doi.org/10.1108/S0733-558X20240000090003 (discussing the evolution of organizational sociology and its continued relevance for understanding the internal dynamics and structural features of organizations).

[57] *See* Linda Smircich, *Concepts of Culture and Organizational Analysis*, 28 ADMIN. SCI. Q. 339 (1983) (discussing how organizational culture theories, adapted from anthropology, inform sociological analyses of authority, identity, and meaning within firms).

[58] *See, e.g.,* Kurt Lewin, *Frontiers in Group Dynamics*, 1 HUM. REL. 5 (1947), https://doi.org/10.1177/001872674700100103 (setting the groundwork for subsequent research into how group behaviors and social interactions shape organizational norms and culture).

[59] *Id.*

[60] *See* Kurt Lewin, *Defining the "Field at a Given Time",* 50 PSYCHOL. REV. 292, 292-310 (1943), https://doi.org/10.1037/h0062738.

[61] *See* Lewin, *supra* note 58.

[62] *See* ABRAHAM H. MASLOW, MOTIVATION AND PERSONALITY (Harper & Row 1954).

[63] *Id.*

exploring in a novel way how bureaucratic environments impact the moral consciousness and actions of managers.[64] He found that culture can generate a form of moral relativism, where ethical standards are contingent on what is acceptable or advantageous in a bureaucratic system at a given moment.[65]

2.3. The Term Corporate Culture Is Coined

Although many aspects of corporate culture were already being studied, it was not until 1951 that the term was coined. Elliott Jaques, a psychoanalyst and organizational theorist, is recognized for being the first to use the term "corporate culture" in his book *The Changing Culture of a Factory* (1951), one of the largest empirical investigations to analyze corporate culture systematically.[66] Jaques recognized corporate culture as the "customary and traditional way of thinking and of doing things" within an organization, which new members must learn and accept to be part of the firm.[67] He worked for years examining the British manufacturing firm Glacier Metal, originating the Glacier Project, and found that organizations develop distinct cultural identities over time, through hierarchical forms, informal norms, and expectations of fairness. Importantly, Jaques emphasized that culture is not only a management tool but a force that influences worker satisfaction.[68] The idea of "felt-fair pay" demonstrated how employees' perceptions of fair compensation influence corporate stability, which validates the role of culture in defining workplace dynamics.[69]

By the 1950s and 1960s, sociologists like Erving Goffman and Philip Selznick further contributed to the understanding of the concept by analyzing how organizational culture constrains

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[64] *See* Robert Jackall, MORAL MAZES: THE WORLD OF CORPORATE MANAGERS (Oxford Univ. Press 1988).

[65] *Id.*

[66] *See* ELLIOTT JAQUES, THE CHANGING CULTURE OF A FACTORY (Tavistock Publ'ns 1951).

[67] *Id.* at 251–52.

[68] *See* Andrew M. Pettigrew, *On Studying Organizational Cultures*, 24 ADMIN. SCI. Q. 570, 570 (1979).

[69] *See generally* ELLIOTT JAQUES, EQUITABLE PAYMENT 2d ed. (Morrison & Gibb 1970); ELLIOTT JAQUES, REQUISITE ORGANIZATION 2d ed. (Cason Hall & Co., Arlington, VA 1996).

and enables employees' behavior.[70] In short, their works helped to reframe corporate culture not as a static construction, but as something that is continually negotiated through interaction and informal social influence.[71] In this way, they recognized that corporate culture does not just reflect formal structures but evolves through the ongoing processes of social influence and power dynamics.[72] Alvin Gouldner (1954) echoed this idea of informal norms, showing that corporate culture is not always aligned with official policies but is heavily influenced by workplace interactions.[73]

Later research then explored the factors that impact the evolution and change of corporate culture. Building upon earlier sociological knowledge, DiMaggio and Powell's seminal 1983 paper on "institutional isomorphism" explained how corporate cultures across different organizations tend to converge due to external pressures.[74] They argued that companies often adopt similar cultural traits not necessarily for efficiency, but because of mimetic (copying others), coercive (due to regulations or legal requirements), and normative (social expectations or industry norms) influences.[75] Another important contribution was made by Harrison White in 1992, whose research on social networks in organizations showed how corporate culture is embedded in relational structures.[76] He emphasized that corporate norms and values emerge from the combination of communication patterns and power relations inside the corporations.[77]

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[70] *See* ERVING GOFFMAN, ASYLUMS: ESSAYS ON THE SOCIAL SITUATION OF MENTAL PATIENTS AND OTHER INMATES 1-38 (Anchor Books 1961) (exploring social dynamics within institutions and offering insights into how social roles and behaviors are shaped, although not directly addressing corporate culture); PHILIP SELZNICK, LEADERSHIP IN ADMINISTRATION: A SOCIOLOGICAL INTERPRETATION 30-35 (Harper & Row 1957) (discussing the concept of institutionalization and how organizational culture develops over time due to leadership and historical context).

[71] *Id.*

[72] *Id.*

[73] *See* ALVIN GOULDNER, PATTERNS OF INDUSTRIAL BUREAUCRACY 1-52 (Free Press 1954) (arguing that informal norms in the workplace often subvert formal organizational policies and influence corporate culture).

[74] *See* Paul J. DiMaggio & Walter W. Powell, *The Iron Cage Revisited: Institutional Isomorphism and Collective Rationality in Organizational Fields*, 48 AM. SOC. REV. 147 (1983), https://doi.org/10.2307/2095101.

[75] *Id.*

[76] *See* HARRISON C. WHITE, MARKETS FROM NETWORKS: SOCIOECONOMIC MODELS OF PRODUCTION (Princeton Univ. Press 1992).

[77] *Id.*

While these scholars advanced the understanding of corporate culture, psychologist Edgar Schein played a pivotal role in formalizing the concept and its elements. Schein's highly influential work on the model of organizational culture broke it down into three levels: artifacts, that are the visible elements such as dress code and office layout; espoused values, which reflect an organization's declared principles; and basic underlying assumptions, the implicit, deeply held assumptions that drive behavior in the company.[78] His model has been widely utilized in corporate culture studies and continues to influence contemporary research and management practices. Schein also emphasized the significant role played by leadership in shaping and consolidating culture and believed that organizational leaders imbue cultural norms through their decisions, communication, and strategic actions.[79] Schein's research changed company culture from a theoretical concept to a systematic and research-based framework that demonstrates how it influences organizational performance, employee engagement, and adaptability to change.[80]

2.4. Corporate Culture in Management and Economics

Despite earlier studies in other fields, researchers in economics started to include corporate culture in their work only in the 1980s, and scholarship in this area remains in development. As Walter Hermalin noted in his 2000 review, although economists had started to take it seriously, many of culture's theoretical frameworks remained underdeveloped and in need of empirical testing.[81] Many reasons may explain the previous neglect. First, culture was deemed irrelevant in economic theory, as it was considered irrational.[82] Second, culture is hard to define and measure, so including it in econometric models was considered problematic.[83] A shift in the focus of

[78] *See* EDGAR H. SCHEIN, ORGANIZATIONAL CULTURE AND LEADERSHIP (Jossey-Bass 1985).

[79] *Id.* at 27-30.

[80] *Id.*

[81] *See* Benjamin E. Hermalin, *Economics & Corporate Culture* 3–5 (Univ. of Cal., Berkeley, Feb. 2000) (unpublished manuscript), https://faculty.haas.berkeley.edu/hermalin/cultchds.pdf (last visited July 7, 2025).

[82] *See* Luigi Guiso, Paola Sapienza & Luigi Zingales, *Does Culture Affect Economic Outcomes?,* 4 J. EUR. ECON. ASS'N 23 (2006), https://doi.org/10.1162/jeea.2006.4.2-3.23 (observing that classical economists treated culture as external and largely irrelevant to economic modeling).

[83] *Id.*

management scholars came with the influential Schein's three-level model of corporate culture, which rapidly gained widespread acceptance in the field.[84] While Schein's early work was rooted in psychology, notably in organizational behavior and group dynamics, his later contributions to management formalized corporate culture as a key to companies' strategic success. His work links psychology and management by demonstrating how well-established cultural assumptions influence leadership, decision-making, and corporate governance in general.[85]

Another major contribution to managerial studies on the topic of corporate culture was by Kotter and Heskett (1992), who explored the relationship between culture and performance.[86] They argued that responsive, customer-focused corporate cultures would tend to perform better than inflexible, bureaucratic cultures,[87] an argument that has influenced corporate strategy, particularly in industries where innovation and rapid change are valued.

Business schools played a significant role in making corporate culture study part of strategic management curricula. Besides Shein, scholars such as Deal and Kennedy formalized culture analysis in organizations, arguing that it is a crucial determinant of firms' success.[88] Therefore, management studies, particularly those influenced by business schools, treat corporate culture as an asset that organizations can design and quantify to enhance their operational performance.

By the 1990s, economists also began incorporating corporate culture into organizational theory, linking it to firm performance and efficiency. David Kreps (1990) included corporate culture in his economic models, asserting that culture is an instrument for maximizing cooperation, trust, and effective decision-making in firms.[89] Krep's work emphasizes how corporate culture enables organizations to address "unforeseen contingencies" by establishing implicit norms of

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[84] *Id.*

[85] *See* Schein, *supra* note 78.

[86] *See* Heskett & Kotter, *supra* note 9.

[87] *Id.*

[88] *See* TERRENCE E. DEAL & ALLAN A. KENNEDY, CORPORATE CULTURES: THE RITES AND RITUALS OF CORPORATE LIFE 25-30 (Addison-Wesley 1982) (exploring the symbolic and behavioral aspects of corporate culture, offering insights into how rituals and shared values shape organizational life).

[89] *See generally* DAVID M. KREPS, *Corporate Culture and Economic Theory*, in PERSPECTIVES ON POSITIVE POLITICAL ECONOMY 90 (James E. Alt & Kenneth A. Shepsle eds., Cambridge Univ. Press 1990).

behavior that guide decision-making in the face of uncertainty.[90] Another well-known author is Jacques Cremer (1993), who contributed to the economic analysis of corporate culture by pointing out its role in coordinating employee expectations and behavior.[91] According to his perspective, corporate culture operates as a common language that enables employee communication and teamwork while minimizing errors and making unnecessary, lengthy contractual agreements.[92] The perspective aligns with transaction cost economics because an effective corporate culture reduces coordination expenses while improving firm operational efficiency.[93]

Other economists, such as Edward Lazear (1995)[94] and Geoffrey Hodgson (1996),[95] have also advanced the understanding of corporate culture. Lazear was concerned with the role of cultural differences in the productivity of employees and the performance of firms, whereas Hodgson focused on the relationship between organizational change and culture, specifically the role played by common values in shaping firm behavior. Olliver Williamson (1985) incorporated corporate culture into transaction cost economics, emphasizing its importance in reducing opportunistic conduct in organizations.[96] Williamson maintained that high-culture firms can achieve lower coordination costs and hence be more resistant to external shocks.[97]

More recently, research in behavioral economics has considered how corporate culture affects employee motivation and decision-making. Richard Thaler and Cass Sunstein's work on nudging establishes how cultural norms affect behavior via the manipulation of implicit "heuristics and biases."[98] Their findings have been applied to corporate governance strategies to improve

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[90] *Id.*

[91] *See* Jacques Crémer, *Corporate Culture and Shared Knowledge*, 6 INDUS. & CORP. CHANGE 351 (1997), https://doi.org/10.1093/icc/6.3.351 (last visited Aug. 6, 2025).

[92] *Id.*

[93] *Id.*

[94] *See* Edward P. Lazear, *Culture and Language*, 107 J. POL. ECON. S95 (1999), https://doi.org/10.1086/250100 (last visited Aug. 6, 2025).

[95] *See* GEOFFREY M. HODGSON, *Corporate Culture and the Nature of the Firm*, in TRANSACTION COST ECONOMICS AND BEYOND 249–69 (John Groenewegen ed., Kluwer Acad. Publishers 1996).

[96] *See generally* OLIVER E. WILLIAMSON, THE ECONOMIC INSTITUTIONS OF CAPITALISM (Free Press 1985).

[97] *Id.*

[98] *See* RICHARD H. THALER & CASS R. SUNSTEIN, NUDGE: IMPROVING DECISIONS ABOUT HEALTH, WEALTH, AND HAPPINESS (Yale Univ. Press 2008) (exploring how cultural norms influence behavior by shaping implicit biases

ethical decisions and compliance.[99] The role of culture in corporate governance was further developed and continues to evolve today. Firms with strong ethical cultures tend to experience fewer regulatory violations and reputational risks.[100] Scholars such as Guiso, Sapienza, and Zingales (2015) have found that companies with high cultural integrity outperform companies that lack it over the long run and enjoy more investor trust.[101]

Based on these studies, it is clear that economists focus mainly on how corporate culture helps lower transaction costs, improve coordination and productivity, and, thereby, increase performance.[102] They perceive culture as a mechanism that assists in integrating employee behavior and corporate goals, minimizing agency problems, and monitoring costs. While economists recognize that corporate culture can evolve, they tend to treat it as a means for improving organizational effectiveness, rather than emphasizing its changeable nature as sociologists do. Economists have played a vital role in expanding the understanding of corporate culture by applying rigorous theoretical and empirical analysis.

2.5. The Legal Approach

Corporate culture gained ground among legal scholars primarily in the 1990s and early 2000s, though some discussions can be traced back to the 1980s. It first emerged in corporate governance and compliance discussions, particularly in the fields of corporate criminal liability, fiduciary duties, and regulatory enforcement.[103] Legal scholars became interested in corporate

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and heuristics, and how these insights are applied to improve decision-making in various contexts, such as policy and corporate governance).

[99] *Id.*

[100] *See* Guiso, Sapienza & Zingales, *supra* note 10 (examining how corporate culture influences firm performance, compliance, and governance, and finding that companies with strong ethical cultures experience fewer instances of corporate misconduct and regulatory violations).

[101] *Id.*

[102] *See* Hermalin, *supra* note 81.

[103] *See, e.g.,* Brent Fisse & John Braithwaite, *Corporate 'Culture' as a Basis for the Criminal Liability of Corporations*, 6 CRIM. L.F. 1 (1995), https://media.business-humanrights.org/media/documents/f72634fd87adfd3d31a22f5f4b93150267b8a764.pdf (exploring how corporate culture contributes to unlawful behavior within firms, emphasizing the need to consider organizational ethos in assessing liability).

culture due to its significant implications for corporate misconduct.[104] Under U.S. law, the doctrine of corporate criminal liability holds corporations criminally responsible for the actions of employees that take place within the scope of their employment and with the purpose of benefiting the corporation.[105] This framework prompted legal scholars to argue that corporate culture, rather than just bad acts by individuals, plays a role in the facilitation of illegal behavior.[106] A pivotal development was the creation of the Federal Sentencing Guidelines for Organizations in 1991, which promoted the use of corporate compliance programs as a means to decrease legal penalties.[107] This challenged scholars to scrutinize the impact of corporate culture on compliance, whether companies actually promote ethical behavior or comply with rules just superficially.[108]

One of the earliest scholars to address corporate culture in legal studies was Christopher Stone (1975), arguing that corporate wrongdoing is typically the result of broader cultural dynamics rather than individual bad conduct.[109] Stone's work paved the way for subsequent debate about corporate responsibility and governance structures.[110] Building upon this foundation, Cynthia A. Williams explored the influence of corporate culture on fiduciary duties and

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[104] *Id.*

[105] *See N.Y. Cent. & Hudson River R.R. Co. v. United States*, 212 U.S. 481, 494–95 (1909) (establishing the principle that corporations may be held criminally liable for the acts of their agents committed within the scope of their employment and for the corporation's benefit).

[106] *See* James Gobert, *Corporate Criminality: Four Models of Fault*, 14 LEGAL STUD. 393 (1994), https://doi.org/10.1111/j.1748-121X.1994.tb00510.x (arguing that corporate culture, reflected in an organization's structures, policies, and practices, can facilitate unlawful conduct beyond individual wrongdoing).

[107] *See* U.S. SENTENCING COMM'N, *The Organizational Sentencing Guidelines: Thirty Years of Innovation and Influence* 3 (2022), https://www.ussc.gov/research/research-reports/organizational-sentencing-guidelines-thirty-years-innovation-and-influence (introducing a framework encouraging organizations to develop compliance programs, with the potential to reduce penalties for corporate misconduct) (last visited Feb. 3, 2025).

[108] *See, e.g.* Kimberly D. Krawiec, *Cosmetic Compliance and the Failure of Negotiated Governance*, 81 WASH. U. L. Q. 487 (2003), https://openscholarship.wustl.edu/law_lawreview/vol81/iss2/8 (arguing that internal compliance mechanisms often serve merely as "window-dressing" rather than genuine deterrents to corporate misconduct) (last visited Aug. 11, 2025).

[109] *See* CHRISTOPHER D. STONE, WHERE THE LAW ENDS: THE SOCIAL CONTROL OF CORPORATE BEHAVIOR (Harper & Row 1975).

[110] *Id.* at 98-102. *See also* James R. Silkenat, *Book Review: Where the Law Ends: The Social Control of Corporate Behavior*, 89 HARV. L. REV. 1645, 1653 (1976); Dale A. Normington, *Book Review: Where the Law Ends: The Social Control of Corporate Behavior*, 1 U. DAYTON L. REV. 275, 278-279 (1976).

governance.[111] She examined how internal cultural factors affect corporate compliance and ethical standards.[112] Similarly, Lawrence E. Mitchell researched the impact of corporate culture on management decision-making and risk-taking.[113] Specifically, Mitchell discussed corporate cultural forces and their influence on fiduciary relations and corporate governance practices.[114]

Furthering the discourse, Jennifer G. Hill intensively investigated the relationship between corporate culture and regulatory compliance, particularly in financial institutions, showing how the former impacts the latter.[115] Additionally, Cristie Ford examined the limitations of relying solely on legal rules to define ethical corporate cultures. She argues that while regulation plays an important role, it is often insufficient to cultivate genuine ethical behavior inside organizations.[116] In other words, compliance may be achieved through law, but integrity requires more than rules—it depends on the culture itself.[117]

In the 2000s, corporate scandals, such as Enron (2001),[118] WorldCom (2002),[119] and the 2008 financial crisis[120] contributed to advance legal interest in corporate culture. The crises exposed widespread corporate governance, risk management, and ethical leadership failures and led scholars to investigate how toxic corporate cultures enable misconduct. They started to

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[111] *See* Cynthia A. Williams, *Corporate Compliance with the Law in the Era of Efficiency*, 76 N.C. L. REV. 1265 (1997), https://scholarship.law.unc.edu/nclr/vol76/iss4/5.

[112] *Id.*

[113] *See* Lawrence E. Mitchell, *Fairness and Trust in Corporate Law*, 43 DUKE L. J. 425 (1993), https://scholarship.law.duke.edu/dlj/vol43/iss3/1.

[114] *Id.*

[115] *See* JENNIFER G. HILL, *Why Did Australia Fare So Well in the Global Financial Crisis?*, in THE REGULATORY AFTERMATH OF THE GLOBAL FINANCIAL CRISIS 203–300 (Eilís Ferran, Niamh Moloney, Jennifer G. Hill & John C. Coffee Jr. eds., Cambridge Univ. Press 2012), https://doi.org/10.1017/CBO9781139175821.004 (discussing how corporate culture in the Australian financial sector influenced regulatory compliance).

[116] *See* Cristie Ford, *New Governance, Compliance, and Principles-Based Securities Regulation*, 45 AM. BUS. L.J. 1 (2008), https://doi.org/10.1111/j.1744-1714.2008.00050.x.

[117] *Id.*

[118] *See* Clinton Wallace Free & Norman B. Macintosh, *Management Control Practice and Culture at Enron: The Untold Story* (2006), https://ssrn.com/abstract=873636 (analyzing how shifts in Enron's corporate culture undermined its management control systems and contributed to the collapse).

[119] *See What Went Wrong at WorldCom?,* Knowledge at Wharton (July 3, 2002), https://knowledge.wharton.upenn.edu/article/what-went-wrong-at-worldcom/ (last visited Feb. 10, 2025)

[120] *See* Saule T. Omarova, *The "Too Big to Fail" Problem*, 103 MINN. L. REV. 2495 (2019), https://scholarship.law.cornell.edu/facpub/1693/).

highlight "culture as a legal risk" in governance and enforcement.[121] Mihailis Diamantis' research suggests that the culture of a corporation should be central in determining corporate liability, given that corporate culture is said to increase compliance more than conventional enforcement instruments.[122]

The scandals and the financial crises also exposed failures in board oversight,[123] raising concerns about the role of leadership in preventing corporate misconduct. This contributed to the strengthening of the "tone at the top" concept,[124] emphasizing that cultural oversight and responsible leadership start with the board and main executives. The Sarbanes-Oxley Act (2002)[125] and the Dodd-Frank Act (2010)[126] reinforced this principle by requiring stronger governance practices, risk management policies, and corporate accountability standards to prevent fraud and misbehavior. The "culture of compliance" debate suggests that courts and regulators should hold boards accountable for fostering ethical environments rather than just implementing compliance mechanisms.[127] Scholars such as Donald C. Langevoort have explored how corporate culture impacts board decision-making and fiduciary duties.[128] He emphasizes that relying solely on top-down directives may be insufficient, as corporate cultures often resist such interventions. In this way, he advocates for a more nuanced approach, one that incorporates behavioral insights to

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[121] *See, e.g.,* Mihailis E. Diamantis, *Corporate Criminal Minds*, 91 NOTRE DAME L. REV. 2049 (2016), https://scholarship.law.nd.edu/ndlr/vol91/iss5/9.

[122] *Id.* at 2054.

[123] *See* Claire A. Hill & Richard W. Painter, BETTER BANKERS, BETTER BANKS: PROMOTING GOOD BUSINESS THROUGH CONTRACTUAL COMMITMENT (Univ. of Chi. Press 2015) (noting that the 2008 financial crisis reflected cultural failures, particularly within leadership, that enabled excessive risk-taking).

[124] *See, e.g.,* Eccles, Ioannou & Serafeim, *supra* note 16; Leo E. Strine, Jr., *Can We Do Better by Ordinary Investors? A Pragmatic Reaction to the Dueling Ideological Mythologists of Corporate Law*, 114 COLUM. L. REV. 449 (2014), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2421480 (discussing further the role of leadership in shaping corporate governance and compliance cultures).

[125] Sarbanes-Oxley Act of 2002, Pub. L. No. 107-204, 116 Stat. 745 (codified as amended in scattered sections of 15 U.S.C.).

[126] Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 1376 (2010) (codified as amended in scattered sections of 12 & 15 U.S.C.).

[127] *See, e.g.,* Donald C. Langevoort, *Cultures of Compliance*, 54 AM. CRIM. L. REV. 933 (2017), https://scholarship.law.georgetown.edu/facpub/1799.

[128] *Id.*

understand how employees actually respond to rules and incentives, so that organizations can more effectively develop a culture of compliance.[129]

Legal scholars have also considered how corporate culture affects criminal intent (*mens rea*) in corporations.[130] Some propose that corporate culture itself should be a factor in determining criminal liability, shifting the attention from specific agents to more general institutional factors.[131] Jennifer Arlen has analyzed how corporate governance structures influence the effectiveness of corporate criminal enforcement.[132]

A more recent driver of corporate culture scholarship has been the rise of environmental, social and governance (ESG) factors. Earlier discussions of corporate culture often arose in the context of Corporate Social Responsibility (CSR), where culture was associated with voluntary commitments or philanthropic efforts.[133] In this framing, culture was seen as a soft mechanism for fostering ethical conduct and goodwill. However, the rise of ESG has brought a more structured and financially material perspective, linking cultural dynamics to measurable sustainability outcomes, risk management, and even regulatory compliance.

Initially developed as an investment screening tool,[134] ESG has since evolved into a comprehensive framework for assessing corporate sustainability practices, and, more recently, into a growing regulatory architecture.[135] This transformation has fueled renewed scholarly interest in

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[129] *Id.*

[130] *See, e.g.,* John C. Coffee Jr., *Gatekeeper Failure and Reform: The Challenge of Fashioning Relevant Reforms*, 84 B.U. L. REV. 301, 305-10 (2004), https://scholarship.law.columbia.edu/faculty_scholarship/520 (discussing how corporate culture influences misconduct and liability); Claire A. Hill, *Why Did Anyone Listen to the Rating Agencies After Enron?*, 4 J. BUS. & TECH. L. 283, 289-92 (2009), https://scholarship.law.umn.edu/faculty_articles/79 (analyzing corporate culture's role in financial crises and governance failures).

[131] *See* Jennifer Arlen, *The Potentially Perverse Effects of Corporate Criminal Liability*, 23 J. LEGAL STUD. 833 (1994), http://www.jstor.org/stable/724468.

[132] *Id.* at 845-50.

[133] *See* DAVID VOGEL, THE MARKET FOR VIRTUE: THE POTENTIAL AND LIMITS OF CORPORATE SOCIAL RESPONSIBILITY 19–27 (Brookings Inst. Press 2005).

[134] *See, e.g.,* Elizabeth Pollman, *The Making and Meaning of ESG*, 14 HARV. BUS. L. REV. 403, 417–18 (2024), U. OF PA., INST. FOR LAW & ECON. RESEARCH PAPER NO. 22-23, EUR. CORP. GOVERNANCE INST.– LAW WORKING PAPER NO. 659/2022 (2022), https://ssrn.com/abstract=4219857 (last visited Mar. 16, 2025) (explaining the evolution of ESG).

[135] For recent regulatory efforts in this area, *See* EUROPEAN COMMISSION, *Corporate Sustainability Reporting Directive (CSRD)*, https://finance.ec.europa.eu/capital-markets-union-and-financial-markets/company-reporting-and-auditing/company-reporting/corporate-sustainability-reporting_en (last visited Mar. 16, 2025); *U.S.* SECURITIES AND

how corporate culture both shapes and reflects a company's ESG commitments. Legal scholars, in particular, have begun to explore how culture influences firms' approaches to sustainability, including environmental responsibility and social issues such as diversity, labor conditions, and stakeholder engagement.

Some scholars advocate for companies to integrate ESG principles into their corporate culture and decision-making processes, as culture has been increasingly linked to corporate accountability and risk management.[136] Studies in this area have also explored the way in which firms with a good ESG culture are doing better on long-term performance.[137] ESG culture has also been at the heart of the controversy on the purpose of a corporation, whether to maximize stock value or to benefit a broader range of stakeholders, including the environment and society.[138] Regardless of where one stands in this debate, corporate culture serves as the backbone that aligns people and systems with a corporation's chosen purpose. Related to this, there is a debate about whether ESG regulations in the United States, specifically climate rules promoted by the Securities and Exchange Commission (SEC), have extended beyond disclosure requirements to include internal governance changes and board-level accountability for fostering ethical corporate behavior.[139]

EXCHANGE COMMISSION, *SEC Adopts Rules to Enhance and Standardize Climate-Related Disclosures for Investors* (Mar. 6, 2024), https://www.sec.gov/newsroom/press-releases/2024-31 (last visited Mar. 16, 2025); CALIFORNIA AIR RESOURCES BOARD, *Information Solicitation to Inform Implementation of California Climate-Disclosure Legislation: Senate Bills 253 and 261, as Amended by SB 219* (Dec. 16, 2024), https://ww2.arb.ca.gov/sites/default/files/2024-12/ClimateDisclosureQs_Dec2024.pdf (last visited Mar. 16, 2025).

[136] *See* Colin Mayer, *The Governance of Corporate Purpose* (EUR. CORP. GOVERNANCE INST., Law Working Paper No. 609/2021, 2021), https://ssrn.com/abstract=3928613 (arguing that boards must embed corporate purpose, culture, measurement, and incentives with ESG-aligned values to ensure accountability).

[137] *See, e.g.,* Eccles, Ioannou & Serafeim, *supra* note 16 (analyzing the correlation between ESG-oriented cultures and long-term performance outcomes); Caroline Flammer, *Corporate Green Bonds*, 142 J. FIN. ECON. 499 (2021), https://doi.org/10.1016/j.jfineco.2021.01.010 (discussing financial benefits of climate commitment).

[138] For recent discussions of corporate purpose, *See generally* Lucian A. Bebchuk & Roberto Tallarita, *The Illusory Promise of Stakeholder Governance*, 106 CORNELL L. REV. 91 (2020), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3581299; Jill E. Fisch & Steven Davidoff Solomon, *Should Corporations Have a Purpose?*, 99 TEX. L. REV. 1309 (2021), https://texaslawreview.org/wp-content/uploads/2021/07/Fisch.Printer.pdf; Edward B. Rock, *For Whom Is the Corporation Managed in 2020? The Debate Over Corporate Purpose*, 76 BUS. LAW. 363 (2021), https://www.ecgi.global/sites/default/files/working_papers/documents/rockfinal.pdf.

[139] *See* CHAMBER OF COM. OF THE U.S. & NAT'L CTR. FOR PUB. POLICY RESEARCH, *Petitioners' Brief Challenging SEC Climate Disclosure Rule* (June 25, 2024), https://corpgov.law.harvard.edu/2024/06/25/the-chamber-and-ncppr-file-brief-challenging-sec-climate-disclosure-rule/ (arguing that the SEC's climate rules are sweeping and

3. What is and What Isn't Corporate Culture

As discussed earlier, corporate culture has been the subject of extensive study across different disciplines, including psychology, sociology, management, economics, and law. As a result, there is no single, universally accepted definition of the term, as a function of the variety of approaches and methodologies of these disciplines. Therefore, the first task of researchers studying corporate culture is to define it in a way that is both sufficient for its richness and analytically helpful.[140] The second challenge is measuring corporate culture in a systematic and objective manner.[141]

Each discipline approaches the topic from its own scientific perspective: psychologists examine cognitive and behavioral processes influencing individual and collective interactions in corporations;[142] sociologists research corporation behavior based on social structures, norms, and networks; economists examine incentives, transaction costs, and organizational efficiency;[143] and legal scholars look at regulating norms, governance practices, and institutions that influence corporate conduct.[144] This fragmentation makes interdisciplinary conversation essential for a more comprehensive understanding of corporate culture and its implications for corporations and society.

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prescriptive, exceeding statutory authority); SIDLEY AUSTIN LLP, *California Places Climate Disclosures Back at the Forefront* (Sept. 19, 2024), https://www.sidley.com/en/insights/newsupdates/2024/09/california-places-climate-disclosures-back-at-the-forefront (describing SB 253 and SB 261 as unprecedented and prescriptive in their requirements for GHG emissions and climate risk reporting).

[140] *See, e.g.,* Grennan & Li, *supra* note 30.

[141] *See* Hermalin, *supra* note 81 (discussing the difficulties in measuring corporate culture from an economic perspective); Nien-hê Hsieh, Benjamin Lange, David Rodin & Mira L. A. Wolf-Bauwens, *Getting Clear on Corporate Culture: Conceptualisation, Measurement and Operationalisation*, 6 J. BRIT. ACAD. s1 155 (2018), https://doi.org/10.5871/jba/006s1.155 (emphasizing the lack of consensus on the definition of corporate culture and complexities in its measurement).

[142] *See, e.g.,* Schein, *supra* note 78 (providing a foundational definition of corporate culture in management and psychology literature).

[143] *See, e.g.,* Williamson, *supra* note 96 (analyzing corporate culture through an economic lens, particularly transaction cost economics).

[144] *See* ROBERT C. ELLICKSON, ORDER WITHOUT LAW: HOW NEIGHBORS SETTLE DISPUTES (Harvard Univ. Press 1991) (exploring how informal norms and cultural factors influence legal and economic behaviors); Jeffrey N. Gordon, *The Rise of Independent Directors in the United States, 1950-2005: Of Shareholder Value and Stock Market Prices*, 59 STAN. L. REV. 1465 (2007), https://scholarship.law.columbia.edu/faculty_scholarship/2933 (discussing corporate governance and cultural shifts in legal frameworks).

Among many definitions, one of the most accepted comes from the famous economist David Kreps, who considers corporate culture as an "intangible asset designed to meet unforeseen contingencies as they arise."[145] This definition approaches corporate culture as an adaptive system to help organizations and their members cope with uncertainty by having a set of shared expectations and informal norms that guide decision-making when formal contracts or incentives are incomplete.[146] Kreps explains that corporate culture works as an implicit governance structure that mitigates agency problems and establishes trust among employees, increasing coordination and efficiency.[147]

Corporate culture refers to the "shared assumptions, values, and beliefs" that guide employee behavior and decision-making in an organization, according to Schein.[148] This determines what is acceptable behavior and what is not, therefore shaping the work environment and influencing organizational outcomes. Gorton and Zentefis describe corporate culture as "the glue that binds employees together and directs their collective behavior at work."[149] In other words, corporate culture has the role of creating cohesion, uniting people under a shared mission, and fostering collective action.

Simplifying the concept, organizational theorists Deal and Kennedy describe corporate culture as "the way things get done around here," which highlights the informal, habitual practices that govern behavior inside a corporation.[150] In a complementary view, psychologist and anthropologist Geert Hofstede characterizes corporate culture as "the collective programming of the mind which distinguishes the members of one organization from another," bringing the idea of shared mental frames that influence behavior and perception.[151] Hill and Jones, from management studies, went beyond these definitions to see corporate culture as "the specific collection of values

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[145] *See* Kreps, *supra* note 89.

[146] *Id.*

[147] *Id.* at 94.

[148] *See* Schein, *supra* note 78, at 12.

[149] *See* Gary B. Gorton & Alexander K. Zentefis, *Corporate Culture as a Theory of the Firm*, ECONOMICA, vol. 91, no. 364 (2024), https://doi.org/10.1111/ecca.12537.

[150] *See* TERRENCE E. DEAL & ALLAN A. KENNEDY, CORPORATE CULTURES: THE RITES AND RITUALS OF CORPORATE LIFE 4 (Addison-Wesley 1982).

[151] *See* GEERT HOFSTEDE, CULTURES AND ORGANIZATIONS: SOFTWARE OF THE MIND 180 (McGraw-Hill 1991)

and norms that are shared by people and groups in an organization and that control the way they interact with each other and with stakeholders outside the organization."[152] This definition shows the external dimension of corporate culture, acknowledging its role in impacting not only internal relationships but also interactions with outside stakeholders such as customers, investors, and regulators.

The scope of such definitions reflects the diverse perceptions relating to corporate culture and its implications. Despite the divergences, the above descriptions depict what could be referred to as the basic aspects of corporate culture. It is a set of values and norms, often intangible, that stimulates cohesion by aligning employees' perspectives and actions with the firm's colleagues and external stakeholders, even in unpredictable situations. Corporate culture involves underlying beliefs and also the actual behaviors that exist in a corporation, even if these happen to deviate from the original principles.[153] Corporate culture reflects the company's purpose and evolves over time due to both internal dynamics and external influences, as this paper will discuss later.[154]

3.1. The Elements of Corporate Culture: What is Said and What is Practiced

To better understand the complexity of corporate culture and its impacts, it is worth further exploring its components. One of the earliest models that attempted to break down corporate culture components was created by Schein and has three levels: artifacts (visible structure and processes), espoused values (stated corporate principles), and basic underlying assumptions (firmly deeply embedded beliefs, difficult to access).[155] This distinction is vital when observing the gap between what a company says its values are and what truly drives behavior in the firm.

Scholars have consistently debated the distinction between espoused values, which are what companies publicly commit to and say they believe in, and their practiced values, which

[152] *See* CHARLES W. L. HILL & GARETH R. JONES, STRATEGIC MANAGEMENT: AN INTEGRATED APPROACH 47 (Houghton Mifflin 2001).

[153] *See infra* Part 3.1.

[154] *See infra* Part 4..

[155] *See* Schein, *supra* note 78, at 25-28.

actually govern day-to-day behavior.[156] The concern is that underlying assumptions, which are difficult for researchers to understand and analyze, may be different from the stated values, therefore defining a culture differently from what the company says. This difference between rhetoric and reality has been a wide area of research in organizational behavior, finance, and law, particularly corporate governance and business ethics. Research has shown that these two elements often diverge, which means discrepancies between a company's public messaging and its internal reality.

In the finance literature, Guiso, Sapienza, and Zingales (2015) examined which dimensions of corporate culture are related to a firm's performance and found that there is a weak correlation between what corporations advertise as their principles and what employees actually perceive them to be[157] They argue that cultural integrity, where stated and practiced values are aligned, is a key driver of corporate success.[158] Building on these findings, Graham, Harvey, Popadak, and Rajgopal (2022) decided to decompose corporate culture into values (ideals that employees and leaders claim to hold) and norms (daily practices through which employees attempt to fulfill these values).[159] They also found that firms' norms, and not the stated values, are the actual mechanisms that define decision-making.[160]

Greenwashing, or "ESG-washing", is a good example of the discrepancy between stated values and actual practices. Some corporations have made strong commitments to sustainability, but continue to engage in business practices that diverge significantly from these claims. For example, large banks announced net-zero carbon goals[161] but continued to finance fossil fuel

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[156] *See, e.g.,* Mohan Gopinath, Aswathi Nair & Viswanathan Thangaraj, *Espoused and Enacted Values in an Organization: Workforce Implications*, 43 MGMT. & LAB. STUD. 277 (2018) https://journals.sagepub.com/doi/full/10.1177/0258042X18797757 (analyzing discrepancies between organizational espoused values and employee awareness, with only 40% of respondents recognizing their firm's stated values).

[157] *See* Guiso, Sapienza & Zingales, *supra* note 10.

[158] *Id.*

[159] *See* Graham et al., *supra* note 11.

[160] *Id.*

[161] *See* NET ZERO ASSET MANAGERS INITIATIVE, https://www.netzeroassetmanagers.org (last visited Feb. 6, 2025).

projects, contrary to their stated ESG commitments.[162] Similarly, various companies released declarations supporting diversity, equity, and inclusion (DEI) in the wake of the Black Lives Matter movement,[163] but progress in leadership diversity and anti-discrimination actions shows that changes are slow, highlighting a gap between commitments and internal cultural values.[164] In another example, some corporations established ambitious carbon neutrality targets but failed to implement operational adjustments to meet them.[165]

When companies do not align their espoused values and their practices, they become exposed to a variety of risks. One is reputational damage, as consumers, investors, non-profit organizations, and other actors are increasingly scrutinizing ESG initiatives.[166] Companies that get caught by overstating their sustainability practices typically face a public backlash, leading to declining consumer trust and investor confidence.[167] Another significant risk is employee disengagement. Workers who believe that there is a disconnect between the values promoted by their firm and the actual practices of their firm may become demotivated, less committed, and more likely to leave. Studies show that when employees see "corporate hypocrisy," productivity decreases and turnover increases.[168] Moreover, companies that do not sustain their publicly stated

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[162] *See* RAINFOREST ACTION NETWORK, *Banking on Climate Chaos: Fossil Fuel Finance Report 2023*, https://www.bankingonclimatechaos.org/; INFLUENCEMAP, *Asset Managers and Climate Change 2022*, https://influencemap.org/report/Asset-Managers-and-Climate-Change-2022. For financial institutions now scaling back their pledges, *See, e.g.,* Todd Cort & Daniel Esty, *Is Net-Zero Banking Dead?*, YALE SCH. OF THE ENV'T (Jan. 15, 2025), https://environment.yale.edu/news/article/net-zero-banking-dead (last visited Feb. 6, 2025) (discussing possible reasons why big U.S. banks are pulling out of the Net-Zero Banking Alliance).

[163] *See* Tiffany Hsu, *Corporate Voices Get Behind 'Black Lives Matter' Cause*, N.Y. TIMES (May 31, 2020, updated June 10, 2020), https://www.nytimes.com/2020/05/31/business/media/companies-marketing-black-lives-matter-george-floyd.html (last visited Feb. 11, 2025) (saying that companies like Nike, Twitter and Citigroup have aligned themselves with the Black Lives Matter movement).

[164] For recent backlash on diversity policies, *See, e.g.,* ASSOC'D PRESS, *These U.S. Companies Are Pulling Back on Diversity Initiatives*, TIME (Jan. 24, 2025, 4:25 PM EST), https://time.com/7209960/companies-rolling-back-dei/ (last visited Feb. 10, 2025)

[165] *See, e.g., Mayanna Berrin v. Delta Airlines Inc.*, No. 2:23-cv-04578 (C.D. Cal. filed May 30, 2023) (lawsuit alleging that Delta's "carbon-neutral" claim was misleading because it relied on ineffective offsets rather than substantive operational emissions reductions)

[166] *See* Stavros Gadinis & Amelia Miazad, *The Hidden Power of Compliance*, 103 MINN. L. REV. 2137, 2203-2205 (2019).

[167] *See* REPRISK, *Greenwashing Risk in ESG Investing: A Closer Look at the Disconnect Between Words and Actions*, https://www.reprisk.com/content/63-news-research/63-2-research/greenwashing-risk-in-esg-investing.pdf.

[168] *See* Nathan Podsakoff et al., *The Effects of Organizational Hypocrisy on Employee Work Attitudes and Behavior*, 105 J. APPLIED PSYCHOL. 1007, 1015 (2020).

ESG commitments may face regulatory and legal consequences.[169] Greenwashing in public disclosures may lead to regulatory sanctions,[170] investor lawsuits, and consumer protection claims under existing securities and consumer laws.[171] Among climate litigation cases against corporations, greenwashing—or "climate-washing"—claims are prevalent and have been achieving successful outcomes.[172]

3.2. The Boundaries of Corporate Culture

Understanding corporate culture also involves distinguishing what it is not. Although corporate culture often comes up in discussions of organizational identity, values, and leadership, it differs from several related concepts that influence businesses but are not corporate culture per se.

First, corporate culture is not just a company's mission statement, code of ethics, or code of conduct. Such documents may state the values that a company wishes to have, but alone, they do not define the culture of an organization. The mission statement may impact culture,[173] but the latter is shaped more through lived experience and patterns of behavior than by written statements,[174] as greenwashing cases have shown. Second, corporate culture is not only a measure of employee commitment or job satisfaction. While high satisfaction can be related to a good

[169] *See Greenwashing Class Action Litigation is An Emerging Risk for Companies*, NAT'L L. REV. (May 2022), https://www.natlawreview.com/article/greenwashing-class-action-litigation-emerging-risk-companies-claims-sustainability; *Mitigating "Greenwashing" Litigation Risk in the U.S. and Beyond*, BEVERIDGE & DIAMOND PC (Apr. 2023), https://www.bdlaw.com/publications/mitigating-greenwashing-litigation-risk-in-the-u-s-and-beyond/.

[170] *See* U.S. SEC. & EXCH. COMM'N, *SEC Charges Public Companies for Misleading ESG Disclosures,* Press Release No. 2023-45 (Mar. 6, 2023), https://www.sec.gov/news/press-release/2023-45.

[171] *See, e.g.,* Lyle Moran, *Climate Lawsuits Against Largest Fossil Fuel Producers Have Almost Tripled*, ESG DIVE (Sept. 25, 2024), https://www.esgdive.com/news/climate-lawsuits-against-largest-fossil-fuel-producers-have-almost-tripled/728069/ (last visited Feb. 8, 2025). For a wider discussion of greenwashing in litigation, *See* Barbara Ballan & Jason J. Czarnezki, *Disclosure, Greenwashing, and the Future of ESG Litigation*, 81 WASH. & LEE L. REV. 545 (2024).

[172] *See* Juliana Vélez-Echeverri, Catherine Higham & Joana Setzer, *Climate-Washing Litigation: Towards Greater Corporate Accountability*, GRANTHAM RSCH. INST. ON CLIMATE CHANGE & ENV'T, LONDON SCH. ECON. & POL. SCI. (Oct. 2023), https://www.lse.ac.uk/granthaminstitute/news/climate-washing-litigation-towards-greater-corporate-accountability/.

[173] *See* Part 3.3 for discussion on corporate purpose v. corporate culture.

[174] *See, e.g.,* Grennan & Li, *supra* note 30.

culture, these are results rather than characteristics of corporate culture itself.[175] An organization may have high employee satisfaction but still have cultural problems, such as a lack of innovation or resistance to change.

Third, corporate culture is not corporate strategy. Strategy establishes the company's business goals in the market, while culture reflects how employees and leadership cooperate to achieve them. A firm with a well-defined strategy may have trouble implementing it if the culture is not aligned with its ambitions. Gibbons, Siegel, and Weber highlight significant distinctions between strategy and culture in the literature.[176] If the primary function of strategy is to guide behavior,[177] then culture can compete with strategy by providing rewards for different behaviors, they say. Besides that, while strategy relies on formal mechanisms, such as planning documents, structured goals, and clearly defined rules, corporate culture is an informal institution that is shaped by shared patterns of behavior over time. In this way, culture is important because it can either support or undermine formal strategies, depending on how aligned the underlying beliefs and practices are with the stated goals.

Another fundamental difference is that strategy is not always long-term in nature and is often updated according to market needs and competitive pressure. Paroutis and Heracleous argue that cultural and strategic misalignment can create internal tensions that harm strategic initiatives,[178] which suggests that strategy must be implemented within a cultural framework that supports it. Van den Steen goes a step further and says that culture is not just an enabling mechanism for strategy but actually delineates and guides strategic choices.[179] Krupskyi and Kuzmytska note that corporate culture can either enable or impede the execution of strategy, as rigid cultures can resist strategic alteration, slowing down adaptation to changes in the market, for

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[175] *See generally* Hill & Jones, *supra* note 152.

[176] *See* Robert Gibbons, John Siegel & Richard A. Weber, *Strategy Meets Culture (for Breakfast): Understanding the Relationship and Highlighting its Potential*, 6 STRATEGY SCI. 111 (2021).

[177] *Id.* at 113.

[178] *See* Sotirios Paroutis & Loizos Heracleous, *Culture vs Strategy: Which to Precede, Which to Align?,* RESEARCHGATE (2013)

[179] *See* Jan Van den Steen, *Culture as a Driver of Strategy*, 9 AM. ECON. J. 1, 1 (2017); Gibbons, Siegel & Weber, *supra* note 176.

example.[180] Alongside that, Barnes says that culture can be a source of competitive advantage and, therefore, an input into strategy rather than a competing force.[181] Furthermore, strategy is more likely to be replicable than culture. Pettigrew observes that business strategies can be copied by firms in the same industry, for example, but corporate culture is deeply ingrained and unique due to its social and historical context. Therefore, culture is a differentiator that competitors cannot easily imitate.[182]

Fourth, corporate culture is different from corporate governance. Governance involves the structures, policies, and processes that direct decision-making at a corporation, whereas culture emerges from shared beliefs and practices that determine how decisions are made and implemented. While corporate governance systems can affect corporate culture, they remain distinct. Corporate governance tools, such as executive compensation,[183] can certainly affect cultural norms by pushing leadership to embrace certain values.[184] For example, companies have linked executive pay to diversity in recent years to prompt leaders to include these values in their decision-making.[185] However, culture is not just the result of governance—it emerges naturally over time through common habits and traditions. Guiso, Sapienza, and Zingales (2015) argue that while governance tools can reinforce cultural elements, they do not solely define them.[186]

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[180] *See* Oleksandr P. Krupskyi & Yuliia Kuzmytska, *Organizational Culture and Business Strategy: Connection and Role for a Company Survival*, 9 CENT. EUR. BUS. REV. 1 (2020).

[181] *See* Jay B. Barney, *Organizational Culture: Can It Be a Source of Sustained Competitive Advantage?,* 11 ACAD. MGMT. REV. 656, 656 (1986).

[182] *See* Andrew Pettigrew, *Understanding Corporate Culture and Its Relation to Strategy,* 6 J. MGMT. STUD. 111, 112 (1988).

[183] *See generally,* Adam B. Badawi & Robert Bartlett, *ESG Overperformance? Assessing the Use of ESG Targets in Executive Compensation Plans*, STANFORD L. & ECON. OLIN WORKING PAPER NO. 592 (Aug. 29, 2024), https://ssrn.com/abstract=4941016.

[184] *Id.*

[185] *See, e.g.,* Maliha Shoaib, *Tapestry Hires First Chief Inclusion and Social Impact Officer*, VOGUE BUSINESS (Apr. 27, 2022), https://www.voguebusiness.com/companies/tapestry-hires-first-chief-inclusion-and-social-impact-officer (noting that the company tied 10 percent of its annual incentive compensation to equity, inclusion, and diversity goals).

[186] *See* Guiso, Sapienza & Zingales, *supra* note 10.

Moreover, corporate culture extends beyond formal rewards in the sense that it reflects deeper, entrenched norms that impact decision-making even in the absence of explicit policies.[187]

Finally, corporate culture is not a synonym of compliance. Compliance requires adherence to external statutes, regulations, and standards applied, so that the company's operations can meet legal and regulatory expectations. In contrast, corporate culture is made up of internal beliefs, values, and behaviors that develop organically inside an organization. While a robust compliance program can define and reinforce aspects of corporate culture, it is not the broad culture itself. A strong compliance culture, supported by leadership commitment, is what research demonstrates is required for effective adherence to regulations. But focusing only on compliance may lead to the risk of the "check-the-box" mentality, where employees follow rules without embracing the values underlying them.[188] This approach can result in superficial compliance that fails to permeate the organization's culture.

Scholarships have also addressed the interaction between regulatory policy and corporate culture. Research shows that a weak integrity culture is a root cause of both operational and financial non-compliance, which suggests that the degree to which an integrity culture permeates an organization has a significant impact on its compliance outcomes.[189] Additionally, corporate fraud studies identify the dangers of a weak ethical culture. These articles demonstrate that firms with a compliance-first, culture-second mindset are more likely to experience fraudulent behavior because their employees may see compliance as a box-ticking exercise rather than an ethical imperative.[190]

For instance, organizations that emphasize compliance checklists without underpinning ethical leadership and accountability structures encourage a culture in which rule evasion can prosper. High-profile corporate fraud cases, such as Enron and Wells Fargo,[191] illustrate how

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[187] *Id.*

[188] *See* Gadinis & Miazad, *supra* note 166.

[189] *See* Dennis Campbell & Tatiana Sandino, *Corporate Governance, Compliance, and Culture: The Role of Integrity in Driving Performance*, 56 J. ACCT. RES. 1, 3 (2018).

[190] *See* Donald C. Langevoort, *The Behavioral Economics of Corporate Fraud*, 65 STAN. L. REV. 1297, 1301 (2013).

[191] *See, e.g.,* JOHN M. CONLEY, ENRON: *The Collapse of Corporate Culture*, in PERSPECTIVES IN BUSS. ETHICS 233 (Laura P. Hartman ed., Mcgraw-Hill 3d ed. 2005); Bethany McLean, *How Wells Fargo's Cutthroat Corporate*

misaligned cultural incentives and weak ethical reinforcement can facilitate pervasive misconduct even when formal compliance mechanisms exist.[192] To mitigate these risks, corporations need to go beyond legal compliance and foster a fraud-deterrent culture, where ethical decision-making is deeply incorporated into day-to-day operations. The implementation of whistleblower protection programs, internal reporting systems, and leadership accountability tools should be used to promote values instead of depending solely on legal threats.[193]

3.3. The ESG-Related Culture

While traditional conceptions of corporate culture have focused on governance, leadership style, risk-taking, and financial decision-making, the rise of ESG has introduced a vital new dimension. ESG seeks to be more than just an investor-driven trend[194] or an emerging regulatory

Culture Allegedly Drove Bankers to Fraud, VANITY FAIR (May 31, 2017), https://www.vanityfair.com/news/2017/05/wells-fargo-corporate-culture-fraud (detailing how a culture of aggressive sales goals and cross-selling incentives led employees to open unauthorized accounts and manipulate customer information).

[192] *See* Miriam H. Baer, *Governing Corporate Compliance*, 50 B.C. L. REV. 949, 952 (2009).

[193] *See* Alexander Dyck, Adair Morse & Luigi Zingales, *Who Blows the Whistle on Corporate Fraud?,* 65 J. FIN. 2213, 2220 (2010).

[194] *See, e.g.,* Brooke Masters, *The Way Forward for ESG*, FIN. TIMES (Sept. 7, 2024), https://www.ft.com/content/7e2c08e6-f9a5-4c51-9957-68d3814ba014 (explaining how major U.S. asset managers such as BlackRock and Vanguard have used proxy voting and public statements to influence corporate behavior on climate, inequality, and diversity); *ESG in 2025: What to Expect in Trump 2.0*, VINSON & ELKINS INSIGHTS (Jan. 15, 2025), https://www.velaw.com/insights/esg-in-2025-what-to-expect-in-trump-2-0/ (noting that U.S. ESG disclosure demands have been driven by the "Big Three," which control 20–30 percent of many companies' stock); BNP Paribas, *Institutional Investors Double Down on ESG, Focus Shifts to Specific Themes, Says BNP Paribas Survey*, ESG NEWS (May 28, 2025), https://esgnews.com/institutional-investors-double-down-on-esg-focus-shifts-to-specific-themes-says-bnp-paribas-survey/ (reporting that 87 percent of institutional investors maintain ESG objectives and focus on themes like energy transition and decarbonization).

mandate.[195] At its core, it aspires to be a cultural commitment to sustainable business practices, often extending beyond what the law requires.[196]

The concept of corporate social responsibility (CSR) has existed for decades, but the twenty-first century has brought a sharper focus on whether sustainability efforts generate tangible business value beyond altruistic motives.[197] This shift toward the "business case" for CSR has reframed debates around "sustainability" and "ESG,"[198] increasingly linking them to risk management, long-term strategic planning, and corporate performance.[199]

The term "ESG" itself emerged from a 2004 initiative led by the United Nations Global Compact, in collaboration with major financial institutions. More precisely, it was coined in 2004 with the release of the United Nations Global Compact Initiative's "Who Cares Wins" report,[200] when the UN Secretary Kofi Annan called upon major financial institutions to examine means through which environmental, social, and governance concerns could be integrated into capital markets.[201] Further dialogue with other market actors, and frameworks promoted by institutions such as the Principle for Responsible Investors (PRI),[202] helped to spread ESG.[203]

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[195] *See generally* Stavros Gadinis & Silvia Fregoni, *Beyond the Brussels Effect: The Surprising Rise of the International Sustainability Standards Board*, J. INT'L ECON. L. (forthcoming 2025) (manuscript on file with authors) (discussing how TCFD and SASB standards influenced the ISSB's development and global adoption). *See also Top 5 ESG considerations for US investors under the Trump-Vance administration*, REUTERS (Feb. 11, 2025), https://www.reuters.com/legal/legalindustry/top-5-esg-considerations-us-investors-under-trump-vance-administration-2025-02-11/ (highlighting how new California statutes like SB 253, SB 261, and AB 1305—and a patchwork of state and federal ESG regulation—are now a central concern for corporate ESG compliance).

[196] *See* Jill E. Fisch, *Making Sustainability Disclosure Sustainable*, 107 Geo. L.J. 923 (2019).

[197] *See* Pollman, *supra* note 134, at 664.

[198] *Id.*

[199] *See* Gadinis & Miazad, *supra* note 166.

[200] *See* THE GLOBAL COMPACT, *Who Cares Wins: Connecting Financial Markets to a Changing World* vii (2004), https://www.unepfi.org/fileadmin/events/2004/stocks/who_ cares_wins_global_compact_2004.pdf.

[201] For a complete history of ESG, *See generally* Elizabeth Pollman, The Making and Meaning of ESG, 14 Harv. Bus. L. Rev. 403 (2024), https://scholarship.law.upenn.edu/faculty_articles/453.

[202] For a complete history of ESG, *See generally* Elizabeth Pollman, *supra* note 134.

[203] *Id.* at 424.

The growing momentum behind ESG has reignited a fundamental debate in corporate law: For whom should corporations be managed, and to whom should they deliver value?[204] The traditional view in corporate law, economics, and management is that the key goal of a corporation is the maximization of profit, which is justified by the premise that shareholders, as residual claimants, take the ultimate financial risk and provide the capital to run the firm.[205] Stakeholder theorists argue, however, that corporations have an obligation to create value for a broader group of stakeholders, including employees, communities, and society at large.[206] Viewed this way, ESG considerations, such as climate responsibility and social impact, are not external constraints of business operations, but part of the corporation's long-term value and even survival.[207]

It is worth noting yet that even in a shareholder-oriented system, corporate managers have some discretion on how profit maximization is to be achieved.[208] Companies compete with each other using different approaches: some prioritize short-term financial gains, while others invest in long-term sustainability and resilience. These strategic decisions are often protected by the business judgment rule, giving corporate leaders the latitude to align ESG priorities with their fiduciary obligations.[209]

In practice, cultivating an authentic ESG culture is increasingly viewed not as optional, but essential to long-term competitiveness. Ride-sharing companies like Uber and Lyft, for example,

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[204] *See* Bebchuk & Tallarita, *supra* note 138.

[205] *See* Michael C. Jensen & William H. Meckling, *Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure*, 3 J. FIN. ECON. 305 (1976); Luigi Zingales, *In Search of New Foundations,* 55 J. FIN. 1623 (2000); Milton Friedman, *The Social Responsibility of Business Is to Increase Its Profits*, N.Y. TIMES MAG., Sept. 13, 1970, at 32.

[206] *See* Lynn A. Stout, *The Shareholder Value Myt*h, 23 STAN. L. & POL'Y REV. 101, 103 (2012), https://ssrn.com/abstract=2277141 (analyzing the connection between agency theory and the shareholder primacy model, and warning that excessive focus on shareholder value may undermine long-term corporate health).

[207] *Id.*

[208] *See, e.g.,* Robert G. Eccles, Ioannis Ioannou & George Serafeim, *The Impact of Corporate Sustainability on Organizational Processes and Performance*, 60 MGMT. SCI. 2835, at 2835 (2014), https://ssrn.com/abstract=1964011.

[209] *See, e.g.,* Adam Badawi, *The Business Judgment Rule*, in ENCYCLOPEDIA OF L. & ECON. 287 (2023) (comparing the wide discretion afforded to directors to negligence standards in force for other professionals, such as doctors); Leo E. Strine, Jr., *The Dangers of Denial: The Need for a Clear-Eyed Understanding of the Power and Accountability Structure Established by the Delaware General Corporation Law*, 50 WAKE FOREST L. REV. 765 (2015) (arguing that Delaware corporate law institutionalizes shareholder primacy by structuring corporate governance to prioritize shareholder interests and limit managerial discretion).

had to address sexual harassment problems as well as the rights of workers to maintain consumer confidence and succeed.[210] Oil companies are investing in cleaner sources of energy not only to please stakeholders but also because they need to stay competitive in the global energy transition process.[211] Similarly, large corporations are now measuring and reporting carbon emissions, setting reduction targets to comply with regulations and to ensure long-term business sustainability.[212]

Therefore, the relationship between ESG and corporate culture is complex and evolving. ESG practices can become ingrained in company culture or remain just superficial commitments to appease external pressures, such as those from investors and consumers.[213] Unlike compliance, which sets minimum standards that companies must follow, many aspects of ESG remain voluntary and, therefore, more reliant on the organization's culture than on formal mandates.

3.4. Why Corporate Culture Matters: Evidence on Impacts and Outcomes

Corporate culture has received increasing attention from scholars. But why does corporate culture matter after all? The short answer, at least from an economic perspective, is that corporate culture is deeply related to many aspects of leaders' decision-making and employee behavior, therefore, defining business outcomes.

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[210] *See, e.g.,* Susan Fowler, *Reflecting on One Very Strange Year at Uber*, SUSAN J. FLOWER BLOG (Feb. 19, 2017), https://www.susanjfowler.com/blog/2017/2/19/reflecting-on-one-very-strange-year-at-uber; Tran Nguyễn, *California Court Rules Uber, Lyft Can Treat Drivers as Independent Contractors*, AP NEWS (July 25, 2024), https://apnews.com/article/california-drivers-uber-lyft-independent-contractors-0aaa5cd01c28d8a575cf1bc3aa3f44a4 (addressing the debates around drivers' rights).

[211] *See, e.g.,* Malcolm Moore, *Eni Bets on Energy Transition Profits to Match Oil and Gas by 2035*, FIN. TIMES (July 28, 2025), https://www.ft.com/content/0fe629d5-f734-4bb6-98df-cda76a7215be (describing how Eni's hybrid entities, Enilive and Plenitude, focus on renewables, biofuels, EV *infra*structure, and retail energy, aiming for parity in profits with its oil-and-gas operations by 2035); Jamie Smyth in New York, *Exxon to Overtake Shell and BP on 'Low-Carbon' Spending*, FIN. TIMES (Apr. 28, 2025), https://www.ft.com/content/ce4da4e0-192a-494a-a1a7-bea940b146f3 (detailing ExxonMobil's $30 billion commitment to low-emission technologies—carbon capture, biofuels, hydrogen, and lithium extraction—as part of its strategy to stay competitive in the evolving energy market).

[212] *See* Yusuf Khan, *Net-Zero Push Is Still On at Many Companies, Standard Setter Says*, WALL ST. J. (June 23, 2025), https://www.wsj.com/articles/net-zero-push-is-still-on-at-many-companies-standard-setter-says-f3bb4066 (noting a 30 percent increase in companies submitting validated climate transition targets in 2025, evidencing ongoing corporate efforts to measure emissions and set goals in response to regulatory and sustainability pressures).

[213] *See Integrating ESG Into Corporate Culture: Not Elsewhere, but Everywhere,* HARV. L. SCH. F. CORP. GOVERNANCE (Mar. 29, 2021), https://corpgov.law.harvard.edu/2021/03/29/integrating-esg-into-corporate-culture-not-elsewhere-but-everywhere/.

Studies have consistently investigated the link between corporate culture and financial performance, often finding a positive relationship. Companies with a well-defined culture demonstrate higher profitability.[214] Similarly, firms that rank high on cultural indicators, such as employee trust, ethical leadership, and mission alignment, outperform competitors in stock market returns, although results can come up just in the long term, given that investors can take time to attribute value to intangibles [215] More specifically, Edmans (2011) found that firms considered as the best places to work, which is an indicator of strong corporate culture, tend to show superior shareholder returns in the long term, implying that cultural values are often underappreciated by the market in the short run.

In addition, corporations that present an "adaptive culture" demonstrate more resilience during economic crises, ensuring long-term financial stability.[216] The study conducted by Guiso, Sapienza, and Zingales (2015) supports this point by showing that companies with high levels of trust and shared values perform better during economic recessions, probably due to their ability to sustain employee productivity and morale.[217] These findings are consistent with Gordon and Zentefis' argument that corporate culture functions as an informal governance mechanism, reinforcing structures that shape financial decision-making and risk management.[218] Additionally, as culture reduces the need for excessive monitoring and control mechanisms because employees internalize firm values and expectations, this leads to more efficient allocation of resources.[219]

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[214] *See* Guiso, Sapienza & Zingales, *supra* note 10.

[215] *See* Alex Edmans, *Does the Stock Market Fully Value Intangibles? Employee Satisfaction and Equity Prices*, 101 J. FIN. ECON. 621 (2011).

[216] *See* David P. Costanza et al., *The Effect of Adaptive Organizational Culture on Long-Term Survival*, 31 J. BUS. & PSYCH. 361 (2016) (examining how adaptive corporate cultures contribute to organizational longevity and resilience over time).

[217] *See* Guiso, Sapienza & Zingales, *supra* note 10.

[218] *See, e.g.,* Gorton & Zentefis, *supra* note 149.

[219] *See* Srikant Datta et al., *Does Firm Culture Influence Corporate Financing Decisions? Evidence from Debt Maturity Choice*, 169 J. BANK. & FIN. 107310 (2024) (finding that strong corporate culture, measured via values like integrity, innovation, teamwork, is associated with shorter debt maturities**,** indicating that a strong culture can substitute for external monitoring, and is linked to higher long-term credit ratings and lower cost of capital).

Lastly, firms that are considered successful in integrating culture into leaders' decisions tend to receive improved investor perception and lower capital costs.[220]

However, a strong culture may also have some drawbacks. For example, if the culture is too rigid, it can discourage dissent opinions and innovation, limiting the company's ability to adapt to market changes, for example.[221] O'Reilly and Chatman (1996) argue that excessive control can also result in "behavior characterized by deviance and personal and social exploitation" in many types of organizations.[222] They also present the idea that a culture that is too cohesive can lead to less strategic flexibility and, therefore, more vulnerability to disruption.[223] Likewise, Denison (1990) suggests that while strong corporate cultures can foster unity and clarity, they may also create resistance to change, harming long-term performance.[224]

There are several interconnected mechanisms by which corporate culture influences financial outcomes. One is that a strong corporate culture tends to increase employee commitment and retention, since they feel part of it, reducing turnover and therefore recruitment costs.[225] When employees are more engaged with the organization, they tend to be more productive and efficient. Another way that culture impacts performance is by aligning decision-making processes, which contributes to ensuring that corporate values guide executive choices.[226]

Moreover, corporate culture improves business performance by playing a crucial role in shaping a firm's reputation and increasing customer trust. When companies employ more customer-focused cultures, they enhance brand loyalty, strengthening consumer confidence and

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[220] *See, e.g.,* Sadok El Ghoul, Omrane Guedhami, Chuck C.Y. Kwok & Dev Mishra, *Does Corporate Social Responsibility Affect the Cost of Capital?*, J. BANK. & FIN. (2010) (empirical evidence from U.S. firms showing that higher CSR scores are associated with lower cost of equity capital, especially through improvements in employee relations, environmental policies, and product strategies).

[221] *See* Graham et al., *supra* note 11.

[222] *See* Charles A. O'Reilly III & Jennifer A. Chatman, *Culture as Social Control: Corporations, Cults, and Commitment*, 18 RES. IN ORG. BEHAV. 187-192 (1996).

[223] *Id.*

[224] *See* DANIEL R. DENISON, CORPORATE CULTURE AND ORGANIZATIONAL EFFECTIVENESS (1990).

[225] *See* Guiso, Sapienza & Zingales, *supra* note 10.

[226] *See* Graham et al., *supra* note 11.

long-term business relationships.[227] Furthermore, corporations that prioritize integrity and accountability are better positioned to avoid governance failures and financial misconduct. This tends to reduce the likelihood of fraud and regulatory problems, reinforcing financial stability and investor confidence.[228] Lastly, culture impacts performance by influencing risk-taking. A strong, performance-driven culture can encourage employees to take calculated risks that lead to innovation and growth, but it can also encourage excessive risk-taking if not properly managed.[229]

4. Taxonomy of Drivers of Culture Change

After establishing the complexity and importance of corporate culture, an essential question remains: How does it change, evolve, or is reshaped over time? While previous sections discussed corporate culture concepts, elements, and the empirical evidence on its impacts on firm outcomes, this turns into a less explored but equally crucial point: the drivers of culture change. Understanding what makes companies alter their norms, values, and behaviors is key for both theoretical development and practical efforts to manage culture effectively.

Based on a careful review of the literature of various disciplines, I argue that corporate culture is not shaped by a single factor but by an interaction of multiple, often overlapping forces. To help researchers and business leaders better understand these factors, this section develops a taxonomy of the catalysts of cultural change, structured around two key dimensions: the source of the driver, whether internal or external to the firm, and the nature of its impact, whether a gradual evolution or a sudden disruption.

Among internal drivers are leadership initiatives, governance structures, compensation systems, and strategic business decisions such as mergers and acquisitions. In turn, external catalysts, which originate outside the firm, involve regulatory shifts, social movements,

[227] O'Reilly III & Chatman, *supra* note 222.

[228] *See* Denison, *supra* note 224.

[229] *See* John R. Graham, Campbell R. Harvey & Manju Puri, *Managerial Attitudes and Corporate Actions*, 69 J. FIN. 1769 (2014) (finding that corporate culture shapes CEO risk preferences, which in turn affect investment and financial policies. In firms with aggressive, high-performance cultures, executives may prioritize short-term gains over long-term stability, increasing exposure to financial distress).

technological developments, and market competition, for example. Some of these forces, like leadership transitions or M&A, may act as sudden shocks moving corporate culture, while others, such as evolving norms or societal changes, bring about more gradual transformations. This taxonomy provides a structured framework for analyzing how diverse influences reshape corporate culture over time.

4.1. Corporate Culture is Not Static

Interdisciplinary research has established that while corporate culture is deeply ingrained in organizations, it is not immutable. Corporate culture is typically described as not static but dynamic in nature,[230] adapting to internal and external pressures. However, while it is widely accepted that culture "can" be altered, there is significant debate about the ease and feasibility of doing so. Most scholars argue that corporate culture change is a difficult task, and some even state that culture is inherently resistant to change.

For instance, Schein emphasizes that changing rooted beliefs is fundamentally a slow process.[231] Some exceptional circumstances might speed up change, but it generally evolves only incrementally over time—and often through re-organization rather than successful individual persuasion.[232] This perspective aligns with the work of Armenakis, Harris, and Mossholder (1993), which states that employee adaptation to change is postulated in theory, but it is always prolonged, challenging, and in some cases even failing.[233] They add that resistance is particularly prevalent where the proposed changes are viewed as socially undesirable.[234] Examples of such resistance are

[230] *See, e.g.,* Grennan & Li, *supra* note 30, at 117.

[231] *See* Schein, *supra* note 78.

[232] *Id.*

[233] *See* Achilles A. Armenakis**,** Stanley G. Harris & K. W. Mossholder, *Creating Readiness for Organizational Change*, 46 HUM. RELAT. 681, 682 (1993) (defining readiness as organizational members' beliefs, attitudes, and intentions as cognitive precursors to change behavior).

[234] *Id.*

evident in periods right after a global economic crisis, where organizations face pushback from their employees when they try to restructure, merge teams, or cut costs.[235]

Empirical examples reinforce this point. Goldman Sachs's identity and practices have persisted despite many attempts at reform, illustrating the inertia of deeply embedded corporate culture.[236] Similarly, after the 2008 financial crisis, many large U.S. banks such as Citigroup and Bank of America attempted to pivot to risk-averse, compliance-focused cultures, but results were mixed, with long-term cultural patterns proving difficult to shift.[237] Both examples are widely documented in the literature as classic illustrations of the challenges of achieving meaningful cultural change in large financial institutions.

Gorton and Zentefis also argue that once a culture is established, especially one shaped by top leadership, it becomes hard to alter it.[238] Kliman, Saxton, and Serpa (1986) add that the likelihood of changing corporate culture depends greatly on how deeply the culture is incorporated.[239] In this way, surface-level norms can be easier to change compared to core, highly rooted values.[240] Hongyi Li and Eric Van den Steen (2021) agree with this perspective and say that "changing an organization's underlying shared beliefs and preferences is challenging and may require drastic measures."[241] Therefore, trying to change norms without tackling the underlying

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[235] *See* Yangmin Tu & Tao Zou, *Organizational Change during Economic Downturns: Psychological Drivers of Employee Resistance and Management Strategies*, 9 ENV'T & SOC. PSYCHOL. 8 (2024), https://doi.org/10.59429/esp.v9i8.2951.

[236] *See* WILLIAM D. COHAN, MONEY AND POWER: HOW GOLDMAN SACHS CAME TO RULE THE WORLD 423–29 (2011) (detailing Goldman Sachs's elite culture and resistance to governance reform);

[237] *See also* Donald C. Langevoort, *The Social Construction of Sarbanes-Oxley*, 105 Mich. L. Rev. 1817, 1825–28 (2007), https://repository.law.umich.edu/mlr/vol105/iss8/6/ (last visited July 30, 2025) (arguing that compliance cultures are often symbolic and hard to embed); Steven A. Ramirez, *Lessons from the Financial Crisis: The Case for a Culture of Compliance*, 1 Wm. & Mary Bus. L. Rev. 225, 238–42 (2010), https://scholarship.law.wm.edu/wmblr/vol1/iss2/2/ (last visited July 30, 2025) (documenting how Citigroup and Bank of America struggled to internalize cultural reforms post-crisis).

[238] *See* Gorton & Zentefis, *supra* note 149, at 7-8.

[239] *See* Ralph H. Kilmann, Mary J. Saxton, and Roy Serpa, *Issues in Understanding and Changing Culture*, 28 CAL. MGMT. REV. 88, 90 (Winter 1986), https://kilmanndiagnostics.com/wp-content/uploads/2018/04/Kilmann_Issues-Culture.pdf.

[240] *Id.* at 91.

[241] *See* Hongyi Li & Eric Van den Steen, *Birds of a Feather … Enforce Social Norms? Interactions among Culture, Norms, and Strategy*, 6 STRAT. SCI. 111, 125 C3 (2021), https://doi.org/10.1287/stsc.2021.0129.

shared beliefs and preferences may be in vain, as the organization will likely revert to the old norms once the pressure is removed.[242]

Compared to societal culture, corporate culture is generally more susceptible to change. Guiso, Sapienza, and Zingales (2002) argue that corporations are more easily reshaped than broader society. However, the tools typically used to drive this change, such as hiring, firing, and promotion decisions, often lead to *ad hoc* adjustments rather than deep, lasting cultural transformation.[243] Researchers like Pettigrew[244] and Tushman and Romanelli[245] have further noted that cultural change occurs more in punctuated bursts, upon crises or strategic shifts, than through a smooth and continuous process.

Finally, factors such as open communication and manager commitment,[246] social culture,[247] and employees' response to change, especially when resistance is low,[248] can facilitate cultural transformation, though the overall process remains complex and challenging.

4.2. Internal Catalysts of Corporate Culture

There are many factors that can potentially change corporate culture. To better understand what we know and what we still need to know about these catalysts, I argue that we can divide

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[242] *Id.*

[243] *See* Luigi Guiso, Paola Sapienza & Luigi Zingales, *Corporate Culture, Societal Culture, and Institutions*, 105 AM. ECON. REV. 336, 337 (2015) (noting that corporate settings allow for more identifiable cultural change in otherwise slow-moving cultural systems).

[244] *See* Andrew Pettigrew, *The Awakening Giant: Continuity and Change in ICI*, 33 J. MANAG. STUD. 107 (1979).

[245] *See* MICHAEL TUSHMAN & PHILIP ROMANELLI, ORGANIZATIONAL EVOLUTION: A METAMORPHOSIS MODEL OF CONVERGENCE AND REORIENTATION (1985).

[246] *See* Richard C. Ringer & Kelly C. Strong, *Managerial Perceptions of Change at a National Laboratory*, 19 LEADERSHIP & ORG. DEV. J. 14 (1998), https://doi.org/10.1108/01437739810368794.

[247] *See* Review of Geert Hofstede, *Culture's Consequences: International Differences in Work-Related Values*, 4 ORG. STUD. 409 (Oct. 1983) (reviewing Geert Hofstede, Culture's Consequences: International Differences in Work-Related Values, 474 pages (Sage 1980)), https://doi.org/10.1177/017084068300400409.

[248] *See* COLLIN CARNALL, MANAGING CHANGE IN ORGANISATION (Prentice Hall 1990); BERNARD BURNES, MANAGING CHANGE: A STRATEGIC APPROACH TO ORGANISATIONAL DEVELOPMENT AND RENEWAL (Pitman 1992); COLIN COULSON-THOMAS, TRANSFORMING THE COMPANY: BRIDGING THE GAP BETWEEN MANAGEMENT MYTH AND CORPORATE REALITY (Kogan Page 1992); JOHN P. KOTTER, LEADING CHANGE (Harv. Bus. Sch. Press 1996).

them into two main categories: internal and external forces. The internal factors include leaders positioning, employees' interactions, corporate governance processes and incentives and the company's historical context. External forces involve economic and political crises, wars, social movements or societal shifts in general, regulatory changes and technological progress. Mergers and acquisitions (M&A) are another potential catalyst and could be categorized as internal or external. However, as M&As are often decided in negotiations conducted just by a few top managers and outside of the daily operations and interactions within the companies, I am including them in external forces.

I also argue that these catalysts can be mainly of two types: shocks and long-term processes. In internal forces, for example, a shock would be a sudden and unexpected change of CEO, while a long-term process would be the routine interactions among employees or the way that leaders support corporate culture over time. Among external forces, an M&A transaction, crises and regulatory changes are examples of shocks, while societal changes and technological progress may be more of a long process than a sudden advent.

4.2.1. Tone at the Top

Leadership is widely accepted to be a key driving internal force shaping and remolding organizational culture. Edgar Schein famously describes leaders as the architects of culture, who embed values and assumptions through what they pay attention to, reward, and tolerate.[249] By articulating a compelling vision and modeling desired behaviors, leaders not only reinforce existing norms but also initiate cultural transformation.[250] John P. Kotter's eight-step model for managing organizational transformation highlights the role of leaders in triggering and institutionalizing culture shifts, from creating urgency and forming coalitions to incorporating new practices in daily routines.[251]

[249] *See generally* Schein, *supra* note 78.

[250] *Id.*

[251] *See* Kotter, *supra* note 248.

In practice, leadership initiatives often serve as a gradual driver of cultural change by setting direction, defining priorities, and modeling values. However, they can also catalyze sudden shocks, particularly when introduced by a new CEO or activist board in response to reputational crises, for instance. The cultural turnaround at Microsoft under Satya Nadella illustrates a gradual, leader-driven transformation.[252] Nadella's appointment as CEO is considered to have marked a turning point in Microsoft's culture, from a rigid and competitive "know-it-all" approach to a more open and collaborative "learn-it-all" mindset.[253] Nadella's leadership was accompanied by internal emphasis on empathy and strategic investments in employee development.[254] Conversely, leadership failures at Wells Fargo during the fake accounts scandal (2016) show how frequent aggressive directives from the top can consolidate toxic norms and trigger governance failures.[255]

The implementation of shock-style reforms can occur during leadership transitions. Following the 2017 revelation of Uber's toxic workplace culture, Dara Khosrowshahi took over as CEO from founder Travis Kalanick to establish a complete transformation of organizational values and accountability systems.[256] Yet, symbolic leadership changes tend to fail when middle managers and consistent incentive alignment don't support them over time.[257]

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[252] *See, e.g.,* Charles A. O'Reilly, *How Microsoft Transformed Its Culture: Five Levers for Organizational Cultural Change*, 4 MGMT. & BUS. REV. 41 (2024), https://doi.org/10.1177/26941058202404010 06 (detailing specific levers, such as mission, values, leadership behaviors, systems, and symbols, used by Nadella and Chief People Officer Kathleen Hogan); Quy Nguyen Huy & Lisa Simone Duke, *Enhancing Innovation Through Organisational Learning and a Culture of Empathy: Microsoft Under CEO Satya Nadella* (INSEAD PUBLISHING case IN1838, 2022), https://publishing.insead.edu/case/enhancing-innovation-through-organisational-learning-and-a-culture-empathy-microsoft-under-ceo-satya-nadella (last visited July 30, 2025).

[253] *See* Satya Nadella, *Hit Refresh: The Quest to Rediscover Microsoft's Soul and Imagine a Better Future for Everyone* 123–24 (2017), https://books.google.com/books?id=SeGMDAAAQBAJ (last visited July 30, 2025).

[254] *Id.*

[255] *See, e.g.,* Emily Glazer, *Wells Fargo CEO John Stumpf Resigns Amid Scandal*, Wall St. J. (Oct. 12, 2016), https://www.wsj.com/articles/wells-fargo-ceo-john-stumpf-retires-1476305934 (last visited July 30, 2025); U.S. Senate Comm. on Banking, Hous. & Urban Affairs, *Wells Fargo: One Year Later* 1–3 (2017), https://www.banking.senate.gov/imo/media/doc/091217%20Wells%20Fargo%20One%20Year%20Later.pdf [https://perma.cc/3M2A-6S6H] (last visited July 30, 2025); Stephen L. Carter, *The Wells Fargo Scandal and the Failure of Corporate Ethics*, 123 Yale L.J.F. 171, 172–75 (2017) (analyzing how incentive structures and weak governance allowed toxic cultural norms to persist).

[256] *See* Susan Fowler, *Reflecting on One Very, Very Strange Year at Uber*, MEDIUM (Feb. 19, 2017), https://www.susanjfowler.com/blog/2017/2/19/reflecting-on-one-very-strange-year-at-uber.

[257] *See* James Detert & Ethan Burris, *Can Your Employees Really Speak Freely?,* HARV. BUS. REV. (Jan.–Feb. 2016).

In addition, the Competing Values Framework by Kim S. Cameron and Robert E. Quinn shows that effective leadership not only initiates cultural transformation but also promotes and sustains the changes by getting structures, policies, and reward systems aligned with it.[258] They classify organizational culture into four: clan (collaborative), adhocracy (creative), market (competitive), and hierarchy (controlling). Effective leaders are the ones who align structures, policies, and rewards with the dominant cultural values to reinforce desired behaviors and ensure that organizational culture is reflected in everyday practices.[259] This enables them to form a culture for long-term development and adaptability. Empirical support for these theoretical propositions is provided by demonstrating that top managers play a central role in managing both the pace and trajectory of cultural change, serving as role models whose actions permeate all tiers of a firm.[260]

4.2.2. Middle Management as Cultural Gatekeepers

While the top–down influence has been accepted as a major agent of corporate culture transformation for many years, several theorists have said that culture is also co-constructed by members at all organizational levels. According to this perspective, cultural change is not a top-down imposition alone; instead, it emerges out of ongoing, bottom–up processes such as recruitment, socialization, and day-to-day interpersonal interaction.

For example, Chatman argues that shared norms and values are primarily a byproduct of collective processes involved in bringing new employees on board and ongoing peer interaction, emphasizing the fact that culture is a working, collaborative construction and not a static artifact, dictated just by C-suite executives.[261] Armenakis, Harris, and Mossholder point out that the success of any attempt to alter culture hinges on employees' willingness and ability to embrace new norms.[262] They indicate that cultural change, when imposed in the absence of grassroots support,

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[258] *See* KIM S. CAMERON & ROBERT E. QUINN, DIAGNOSING AND CHANGING ORGANIZATIONAL CULTURE (Prentice Hall 1999).

[259] Id

[260] *See infra* Part 5.3.

[261] *See* SANDRA E. CHATMAN, MATCHING PEOPLE AND ORGANIZATIONS: SELECTION AND SOCIALIZATION IN PUBLIC ACCOUNTING FIRMS (1991).

[262] *See* Armenakis, Harris & Mossholder, *supra* note 233.

tends to meet with significant resistance, implying that the diffusion of new cultural habits is no less a bottom-up process than one driven by top-management initiatives.[263] Similarly, Pettigrew argues that cultural transformation, often emerging from punctuated bursts, is driven not only by deliberate strategies designed by leaders but also by unofficial forces that reflect the collective experience of employees.[264] Together, these perspectives describe that effective cultural transformation is about the multiple internal forces at play, recognizing that everyday interactions among employees are important to the evolution of the corporate culture.

In this way, middle management may also be a driver of culture change. While leadership sets strategic direction and symbolic tone, middle management plays a crucial gatekeeping role in translating cultural aspirations into daily routines. These actors operate at the intersection of corporate vision and frontline execution. They interpret leadership messages, prioritize implementation, and model behavior for their teams. As such, middle managers are often the filter through which organizational culture is transmitted, reinforced, or challenged.[265]

Some research on compliance and ethics programs emphasizes that successful cultural transformation depends not only on "tone at the top," but also on "tone in the middle."[266] That is, middle management buy-in is critical for initiatives like ethics training, DEI implementation, or new reporting structures to take hold. Without alignment at this level, even well-intentioned reforms risk becoming symbolic rather than substantive.[267] Middle managers are also often best positioned to identify informal norms or "workarounds" that undermine official policies, a dynamic particularly visible in large and hierarchical organizations.[268]

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[263] Id

[264] *See* Pettigrew, *supra* note 244.

[265] *See* Ethan Burris & James R. Detert, *Can Your Employees Really Speak Freely?*, Harv. Bus. Rev. (Jan.–Feb. 2017), https://hbr.org/2017/01/can-your-employees-really-speak-freely [https://perma.cc/8ZUG-HTJE] (last visited Aug. 1, 2025) (noting middle managers' gatekeeping function in shaping feedback channels and voice climate).

[266] *Id.*

[267] *See* Todd Haugh, *The Power Few of Corporate Compliance*, 53 Ga. L. Rev. 1287, 1317–24 (2019), https://digitalcommons.law.uga.edu/glr/vol53/iss5/5/ [https://perma.cc/6UVZ-KMQ8] (last visited Aug. 1, 2025) ("Compliance officers often face resistance from mid-level managers whose incentives remain tied to performance, not integrity.").

[268] *See* Donald C. Langevoort, *Cultures of Compliance*, 54 Am. Crim. L. Rev. 933, 939–41 (2017), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2879311 (last visited Aug. 1, 2025) ("Middle managers serve as

Middle managers have become even more important now that more people work remotely, companies have fewer management layers, and performance is tracked closely with data tools.[269] When empowered, they can act as micro-leaders of cultural evolution; when disengaged, they may resist change, preserve legacy behaviors, or dilute leadership messages.[270] Thus, companies seeking to drive meaningful change increasingly invest in middle-management engagement, coaching, and incentive alignment.[271] "The 'tone in the middle' is a powerful determinant of whether rank-and-file employees internalize ethical norms or treat them as formalities."[272]

4.2.3. Tone at the Bottom and Employee-Driven Cultural Change

Although most scholarly and regulatory focus has traditionally been on the "tone at the top," and more recently on the "tone in the middle," a newer concept gaining attention is the "tone at the bottom," the informal norms and expectations shaped by frontline employees.[273] These actors often interpret, adapt, or resist top-down cultural messages in ways that significantly affect implementation.

Bottom-up influence is particularly visible in decentralized organizations, retail operations, and platform companies where thousands of employees interact directly with customers or suppliers.[274] These employees may uphold ethical standards even when leadership fails, or conversely, reinforce toxic subcultures despite reform efforts from above. For example, research

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both translators and enforcers of organizational values, and their interpretation of compliance priorities often determines how seriously such efforts are perceived by subordinates.").

[269] *Id.*

[270] *See* Ben W. Heineman, Jr., *Inside the Mind of the Monitor*, YALE L.J. FORUM 105 (2010), https://www.yalelawjournal.org/forum/inside-the-mind-of-the-monitor (last visited Aug. 1, 2025) (discussing how monitors focus on mid-level management commitment as a proxy for sustainable compliance).

[271] *See* Hui Chen & Eugene Soltes, *Why Compliance Programs Fail—and How to Fix Them*, HARV. BUS. REV. (Mar.–Apr. 2018), https://hbr.org/2018/03/why-compliance-programs-fail-and-how-to-fix-them (last visited Aug. 1, 2025) (stressing the need to engage middle managers in compliance ownership rather than viewing them as passive implementers).

[272] *See* Langevoort, *supra* note 268, at 939.

[273] *See* Dana Radcliffe, *What "Tone at the Bottom" Means for Ethical Culture*, CORNELL SC JOHNSON COLLEGE OF BUS. (Apr. 11, 2017), https://business.cornell.edu/hub/2017/04/11/tone-bottom-ethical-culture/.

[274] *See* Ethan Bernstein, *The Transparency Trap*, HARV. BUS. REV. (Oct. 2014), https://hbr.org/2014/10/the-transparency-trap.

on Wells Fargo has shown how intense pressure and informal norms among branch-level employees contributed to the creation of fake accounts, even when upper management publicly disavowed such behavior.[275] In contrast, companies like Costco and Patagonia have been praised for cultivating strong pro-social cultures at the front lines, where workers internalize mission-driven values.[276] These examples suggest that bottom-up dynamics deserve closer integration into cultural change frameworks, especially as employees increasingly use social media, collective action, and whistleblowing to voice social concerns.[277]

In some cases, bottom-up cultural influence manifests when employees challenge what they perceive as value failures. The #GoogleWalkout, for instance, mobilized thousands of workers to protest the company's handling of sexual harassment claims, prompting tangible governance reforms, including changes to arbitration policy.[278] Similarly, whistleblower Susan Fowler's 2017 blog post exposing toxic workplace practices at Uber catalyzed an internal investigation, the resignation of then-CEO Travis Kalanick, and a broader effort to reset the company's culture.[279] In both cases, employees operated outside formal compliance structures, suggesting that cultural change can originate from disempowered actors when some values are at stake.

Research in organizational theory also says that corporate culture is not merely dictated from the top, but "interpreted and enacted" by employees throughout the hierarchy.[280] When day-to-day practices at the operational level diverge from official policies, bottom-up norms can become powerful countercurrents—either reinforcing cultural commitments (e.g., frontline

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[275] *See* Stephen Gandel, *Wells Fargo's Culture Was the Root Cause of Its Scandal*, FORTUNE (Apr. 10, 2017), https://fortune.com/2017/04/10/wells-fargo-fake-accounts-culture/.

[276] *See* ROBERT I. SUTTON & HUGGY RAO, SCALING UP EXCELLENCE: GETTING TO MORE WITHOUT SETTLING FOR LESS 45–47 (2014); Jennifer Goodman, *The Secrets Behind Patagonia's Culture of Activism*, SHRM (Apr. 21, 2022), https://www.shrm.org/resourcesandtools/hr-topics/employee-relations/pages/secrets-behind-patagonias-culture-of-activism.aspx.

[277] *See* Roy Shapira, *Law and Reputation*, 90 U. CHI. L. REV. 528, 530–38 (2023).

[278] *See* Kate Conger & Daisuke Wakabayashi, *Google Walkout: Employees Stage Protest Over Handling of Sexual Harassment*, N.Y. TIMES (Nov. 1, 2018), https://www.nytimes.com/2018/11/01/technology/google-walkout-sexual-harassment.html.

[279] *See* Mike Isaac, *Uber's C.E.O. Resigns Under Pressure*, N.Y. TIMES (June 21, 2017), https://www.nytimes.com/2017/06/21/technology/uber-ceo-travis-kalanick.html [https://perma.cc/85WS-ZJ7S] (last visited July 31, 2025).

[280] *See* Jodi L. Short & Michael W. Toffel, *Making Self-Regulation More Than Merely Symbolic: The Critical Role of the Legal Environment*, 55 ADMIN. SCI. Q. 361, 369–71 (2010).

enthusiasm for customer service at Southwest Airlines)[281] or eroding them through cynicism, shortcuts, or passive resistance.[282]

Moreover, employee activism increasingly intersects with generational shifts. Younger workers often expect alignment between corporate purpose and values, especially around ESG issues.[283] This has translated into internal pressures at companies like Amazon, Facebook (now Meta), and Netflix, where internal petitions and public letters have challenged leadership on issues ranging from warehouse conditions to misinformation and climate impact.[284]

Despite its growing relevance, "tone at the bottom" remains difficult to measure and influence. Legal and managerial mechanisms to channel this influence, such as protected whistleblowing frameworks and anonymous feedback tools, remain underdeveloped in many firms.[285] Additionally, structural power asymmetries and fear of retaliation undermine these initiatives.[286] Without psychological safety and clear feedback loops, employees may self-censor, disengage, or resort to external channels like media or litigation—undermining internal trust.[287]

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[281] *See* Walter Frick, *How Southwest Airlines' Culture Drives Success*, HARV. BUS. REV. (Jan. 4, 2016), https://hbr.org/2016/01/how-southwest-airlines-culture-drives-success [https://perma.cc/4GG8-9HSF] (last visited July 31, 2025).

[282] *See* MARCIA P. MICELI, JANET P. NEAR & TERRY M. DWORKIN, WHISTLE-BLOWING IN ORGANIZATIONS 54–58 (Routledge 2008).

[283] *See* SARAH A. SOULE, SOCIAL MOVEMENTS AND ORGANIZATIONAL THEORY 207–09 (Cambridge Univ. Press 2005).

[284] *See, e.g.,* Julia Kollewe, *Amazon Workers in 20 Countries to Protest or Strike on Black Friday*, THE GUARDIAN (Nov. 25, 2024), https://www.theguardian.com/business/2024/nov/25/amazon-protest-strike-black-friday (describing how Amazon workers across more than 20 countries launched coordinated protests—including delivering a petition with over 110,000 signatures—to demand better labor rights and environmental sustainability); *Meta Employees Question Company's Removal of Posts on Internal Forum: 'This Is a Free Speech Issue'*, BUSINESS INSIDER (Feb. 2025), https://www.businessinsider.com/meta-employees-question-removal-internal-forum-post-2025-2 (reporting that Meta staff formed a group called CEE Watch to document and push back against internal post removals related to sensitive topics, signaling employee activism over leadership policies).

[285] *See* Michael Volkov, *The Importance of Tone at the Bottom*, VOLKOV LAW GROUP BLOG (May 11, 2015), https://blog.volkovlaw.com/2015/05/the-importance-of-tone-at-the-bottom/ [https://perma.cc/5DF6-V9TN] (last visited July 31, 2025).

[286] *See* MARCIA P. MICELI, JANET P. NEAR & TERRY MOREHEAD DWORKIN, WHISTLE-BLOWING IN ORGANIZATIONS 47–53 (2008); Elizabeth Tippett, *The Legal Implications of Internal Reporting Systems*, 50 AM. BUS. L.J. 1, 23–27 (2013).

[287] *See* AMY C. EDMONDSON, THE FEARLESS ORGANIZATION: CREATING PSYCHOLOGICAL SAFETY IN THE WORKPLACE FOR LEARNING, INNOVATION, AND GROWTH 102–107 (2018).

Yet as cultural legitimacy becomes increasingly reputational and stakeholder-driven, organizations that fail to engage with bottom-up perspectives risk cultural dissonance and external backlash.[288]

4.2.4. Incentives

Incentives, part of the corporate governance mechanisms, can also be significant catalysts for cultural change by connecting employee behavior with the firm's strategic goals. Incentive systems complement leadership by institutionalizing cultural priorities. These mechanisms shape culture gradually by defining what is rewarded, tolerated, or punished. However, abrupt shifts in incentives, such as when regulators or investors pressure companies to link pay to ESG outcomes, can generate sudden changes in employee behavior.

Economic thinkers recognize that incentives tied to performance, such as bonuses, stock options, and profit-sharing plans, can be powerful tools to encourage support for a new envisioned culture. The Enron scandal remains the canonical example of incentives driving destructive culture, as overly aggressive bonus structures prioritized short-term profits over ethical conduct.[289] Conversely, Johnson & Johnson's Credo, which has guided incentive and reward systems for decades, illustrates how incentive structures aligned with core values can sustain a culture of responsibility.[290]

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[288] *See* Roy Shapira, *supra* note 277 (arguing that reputational intermediaries, including employees and media, shape corporate behavior in ways that law alone cannot); LAUREN EDELMAN, WORKING LAW: COURTS, CORPORATIONS, AND SYMBOLIC CIVIL RIGHTS 217–22 (2016) (describing how internal legitimacy among employees interacts with external perceptions); JULIE COHEN, BETWEEN TRUTH AND POWER: THE LEGAL CONSTRUCTIONS OF INFORMATIONAL CAPITALISM 221–24 (2019) (discussing stakeholder pressure, legitimacy, and corporate adaptation in the digital age).

[289] *See* Jeffrey N. Gordon, *What Enron Means for the Management and Control of the Modern Business Corporation: Some Initial Reflections*, 69 U. Chi. L. Rev. 1233 (2002), https://chicagounbound.uchicago.edu/uclrev/vol69/iss3/17/ (last visited July 30, 2025); Frank Partnoy, *Enron and the Derivatives Time Bomb*, 60 WASH. & LEE L. REV. 1033, 1051–53 (2003), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=302332 (explaining how bonus-driven accounting practices fueled Enron's collapse).

[290] *See* JOHNSON & JOHNSON, *Our Credo* (rev. June 2018), https://www.jnj.com/credo/ [https://perma.cc/8FD9-6M73] (last visited July 30, 2025) (describing Johnson & Johnson's long-standing values-based management framework); Joanne B. Ciulla, *Integrity and Johnson & Johnson's Credo*, 58 BUS. & SOC'Y REV. 249, 252–55 (2003) (arguing that Johnson & Johnson's Credo-aligned incentive systems help sustain ethical corporate culture).

Gibbons and Henderson's research shows how compensation structure changes can make individual work efforts match organizational objectives, which creates an organizational culture that supports the new strategic direction.[291] Gorton and Zentefis further demonstrate that corporate culture can function as an internal organizing principle, reducing the necessity for formal agreements and market-coordinating systems.[292] According to their perspective, a strong corporate culture can act as a substitute for transaction control mechanisms because it directs employee conduct toward strategic goals through internal alignment rather than needing external arrangement enforcement.[293]

Milgrom and Roberts note, however, that if cultural changes are to be lasting, organizational structures also need to change along with any shift based on incentives.[294] Structural changes in processes and systems, for example, are important to ensure that the incentives are supported and sustainable, making the intended culture enter the organization's operations.[295] A clear example of this dynamic can be found in IBM's cultural shift during its transition to cloud services and AI solutions in the 2010s. As the company moved away from its traditional hardware-centered model, it sought to foster a more agile, innovative, and customer-focused culture. Incentive structures were redesigned to reward cross-unit collaboration and client-centered outcomes, encouraging employees to break from product silos.[296] To support this, IBM implemented key structural reforms: it reorganized its business units around industry verticals rather than technologies, created client innovation centers to facilitate experimentation, and embedded design thinking across teams.[297] These structural adjustments were critical to

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[291] *See* Robert Gibbons & Rebecca Henderson, *Relational Contracts and Organizational Capabilities*, 26 J. ECON. PERSP. 245 (2012).

[292] *See* Gary B. Gorton & Alexander K. Zentefis, *Corporate Culture as an Organizational Mechanism*, 34 J. FIN. ECON. 102 (2022).

[293] *Id.*

[294] *See* PAUL MILGROM & JOHN ROBERTS, ECONOMICS, ORGANIZATION, AND MANAGEMENT (1990).

[295] *Id.*

[296] *See* David Kiron et al., *The Cultural Benefits of Becoming a Data-Driven Organization*, MIT SLOAN MGMT. REV. (Feb. 11, 2019), https://sloanreview.mit.edu/article/the-cultural-benefits-of-becoming-a-data-driven-organization/ (discussing IBM's cultural and structural transformation to support innovation and client-centricity).

[297] *See* Jon Iwata, *IBM's Cultural Revolution: A Study in Strategic Transformation*, HARV. BUS. REV. (Sept. 2018), https://hbr.org/2018/09/ibms-cultural-revolution (describing how IBM embedded design thinking and reorganized business units to align with its cloud and AI strategy).

reinforcing the new culture and making the strategic transformation. Therefore, while incentive systems can create great shifts in behavior, their success often depends on complementary organizational changes that reinforce the new dynamics.[298]

4.2.5. Governance Structures and Organizational Processes

Governance structures, such as board oversight, audit systems, risk management protocols, compliance programs, and internal reporting systems, also play an important role in shaping corporate culture. These mechanisms institutionalize behavioral expectations and accountability norms and are likely to impact culture gradually, incorporating values into routines and control structures over time.

Consider, for example, how Wells Fargo's internal sales supervision and weak escalation channels allowed problematic norms to persist until external scrutiny forced governance reform;[299] or how General Electric's historical reliance on financial targets and opaque internal reporting became implicated in cultural critiques that contributed to later restructuring.[300] By contrast, firms that strengthened audit committees and whistleblower protections post-crisis (e.g., JPMorgan Chase) illustrate how process redesign can slowly recalibrate norms of accountability.[301]

Theoretical frameworks, especially from law and organizational theory, emphasize this function of corporate governance. For example, the agency theory says that corporate governance

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[298] *See* JEFFREY PFEFFER, LEADERSHIP BS: FIXING WORKPLACES AND CAREERS ONE TRUTH AT A TIME 97–103 (2015).

[299] *See* James E. McNulty & Aigbe Akhigbe, *Corporate Culture and Bank Financial Performance: A Case Study of the Wells Fargo Sales Practices Scandal* (FLORIDA ATLANTIC UNIV. COLLEGE OF BUS. ADMIN. Working Paper, Jan. 31, 2025), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=5279156 (last visited July 30, 2025) (analyzing how unrealistic sales targets, weak escalation protocols, and incentive pressures fostered systemic unethical behavior and cultural dysfunction at Wells Fargo).

[300] *See* Lawrence A. Cunningham, *General Electric's Financial House of Cards*, 45 J. Corp. L. 761, 772–75 (2020) (analyzing GE's over-reliance on financial targets and opaque internal reporting).

[301] *See* Jill E. Fisch & Cindy A. Schipani, *Reconsidering the Board's Duty to Monitor Risk*, 32 Del. J. Corp. L. 725, 742–48 (2007) (discussing how strengthened audit committees and whistleblower protections—e.g., at JPMorgan Chase—help recalibrate norms of accountability); *JPMorgan to Spend $4 Billion on Compliance and Risk Controls: WSJ*, Reuters (Oct. 10, 2013), https://www.reuters.com/article/business/jpmorgan-to-spend-4-billion-on-compliance-and-risk-controls-wsj-idUSBRE98C007/ (last visited July 31, 2025) (reporting JPMorgan's plan to add ~5,000 staff and billions in spending to bolster risk and compliance after regulatory investigations).

structures are designed to align managers (agents) and shareholders (principals) interests, which is key for reducing agency costs.[302] Although economic in its formulation, this alignment between managers and shareholders also operates at the cultural level, incorporating responsibilities and discipline into the firm's standards of operation. Consistently, stewardship theorists argue that governance structures, if properly developed, not only constrain behavior but also facilitate values-based management culture guided by professional ethics and trust.[303]

Beyond theory, empirical research confirms that governance structures shape corporate culture. A study found that firms with strong governance, such as strong boards and tight internal controls, are more likely to have cultures that focus on long-term value creation and accountability.[304] Governance failures, however, seem to go along with cultures that tolerate risk, short-termism, or misconduct. A glaring example is the collapse of Lehman Brothers during the 2008 financial crisis.[305] Governance failures, such as a weak board oversight, uncontrolled risk-taking by executives, and the use of deceptive accounting practices, allowed a culture of excessive leverage and short-term gains that ultimately contributed to the firm's demise.[306]

While governance structures are more likely to drive slow cultural evolution, they can also become drivers of rapid change, particularly after major crises. For example, legal or reputational failures can prompt structural reforms, with the imposition of new compliance requirements, and force companies to quickly reexamine internal values and behavioral opportunities. Regulatory interventions (e.g., Sarbanes-Oxley Act,[307] Dodd-Frank Act[308]) have consistently required formal changes in board composition, auditing practices, and disclosure policies, causing not only

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[302] Jensen & Meckling, *supra* note 205.

[303] *See* Lex Donaldson & James H. Davis, *Stewardship Theory or Agency Theory: CEO Governance and Shareholder Returns*, 16 AUSTL. J. MGMT. 49 (1991)

[304] *See* Guiso, Sapienza, and Zingales, *supra* note 10.

[305] *See* ANTON R. VALUKAS, LEHMAN BROTHERS HOLDINGS INC. CHAPTER 11 PROCEEDINGS EXAMINER'S REPORT, Vol. 1 (Mar. 11, 2010).

[306] *See* Lynne L. Dallas, *Short-Termism, the Financial Crisis, and Corporate Governance*, 37 J. CORP. L. 265 (2012).

[307] *See* SARBANES–OXLEY ACT of 2002, Pub. L. No. 107-204, 116 Stat. 745.

[308] *See* DODD–FRANK WALL STREET REFORM AND CONSUMER PROTECTION ACT, Pub. L. No. 111-203, 124 Stat. 1376 (2010).

procedural change but deeper cultural change. In these instances, culture change is institutionalized through systematic governance reform that reshapes the routines, accountabilities, and incentive structures that define daily organizational life.

4.2.6. Mergers and Acquisitions

Mergers and acquisitions (M&A) decisions, though often catalyzed by market forces, are internal strategic actions that significantly impact culture. These transactions combine distinct teams and organizational values, requiring the alignment—or re-engineering—of cultural practices.[309] Globalization further complicates and enriches this scenario because businesses have to build a corporate identity while dealing with unities in diverse places and markets in the world.[310] M&A can function as a cultural shock, demanding rapid integration, or as slower processes shaped by post-deal organizational routine, often involving not just top executives but also lower-level employees interacting with new teams. Research suggests that cultural integration is essential for M&A success, and when done deliberately, can be a powerful mechanism for transformation.[311]

There is no shortage of examples. The Daimler–Chrysler combination famously struggled with national and managerial culture clashes.[312] The Disney–Pixar acquisition showed how preserving creative subcultures under a larger governance umbrella can enable successful integration.[313] More recently, Amazon–Whole Foods highlighted how a performance- and technology-driven acquirer can modify aspects of a mission-oriented retailer's decision-making and data practices.[314]

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[309] *See* Pettigrew, *supra* note 244.

[310] *See, e.g.,* Theodore Levitt, *The Globalization of Markets*, 56 HARV. BUS. REV. 92 (1983); C. A. BARTLETT & S. GHOSHAL, MANAGING ACROSS BORDERS: THE TRANSNATIONAL SOLUTION (Harv. Bus. Sch. Press 1992); GEERT HOFSTEDE, CULTURES AND ORGANIZATIONS: SOFTWARE OF THE MIND (McGraw-Hill 2001).

[311] *See, e.g.,* Cartwright, Sue & Cooper, Cary L., MANAGING MERGERS, ACQUISITIONS AND STRATEGIC ALLIANCES: INTEGRATING PEOPLE AND CULTURES (2d ed. 2012).

[312] *See* Steven M. Davidoff & Christina M. Sautter, *Lock-Up Creep*, 38 J. Corp. L. 681, 693–96 (2013) (discussing Daimler–Chrysler cultural clashes).

[313] *See* Boris Groysberg & Michael Slind, *Disney–Pixar: Preserving the Magic*, Harv. Bus. Sch. Case 9-709-462 (2009).

[314] *See* Dennis Campbell, Tatiana Sandino, James Barnett & Christine Snively, *Whole Foods Under Amazon* (Harv. Bus. Sch. CASE 118-074, Mar. 2018) (rev. July 2018),

4.2.7. Organizational Norms and History

A company's history, symbols, and rituals, accumulated over time and reinforced by repetition, distinguish one firm from another, even inside the same industry and geographic region. They are what make each company unique. These elements constitute deep layers of corporate culture, which give each firm its distinct identity.[315] They also serve as organizational memory and reflect what scholars call the "imprinting" effect, which states that formative experiences and structures shape long-term behavior.[316] Because of this, rather than being easily replaced, these cultural foundations evolve gradually and serve as interpretive lenses through which new initiatives are evaluated. They also determine what some authors describe as a firm's ability to accommodate ambiguity and integrate new strategic directions.[317] In this way, entrenched cultural patterns condition an organization's absorptive capacity for new norms,[318] shaping whether change is embraced, adapted, or rejected.

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https://www.hbs.edu/faculty/Pages/item.aspx?num=54309 (last visited July 31, 2025); Katie Tarasov, *Amazon Bought Whole Foods Five Years Ago for $13.7 Billion. Here's What's Changed at the High-End Grocer*, CNBC (Aug. 25, 2022), https://www.cnbc.com/2022/08/25/how-whole-foods-has-changed-in-the-five-years-since-amazon-took-over.html (last visited July 31, 2025).

[315] *See* Schein, *supra* note 78.

[316] *See* MICHAEL T. HANNAN, GLENN R. CARROLL & LÁSZLÓ PÓLOS, LOGICS OF ORGANIZATION THEORY: AUDIENCES, CODES, AND ECOLOGIES 56–58 (2007) (discussing organizational "imprinting" and inertia).

[317] *See* C. Marlene Fiol & Edward J. O'Connor, *Waking Up! Mindfulness in the Face of Bandwagons*, 23 ACAD. MGMT. REV. 54, 56–58 (1998) (exploring how organizations absorb or resist new information and strategic change).

[318] *See* Wesley M. Cohen & Daniel A. Levinthal, *Absorptive Capacity: A New Perspective on Learning and Innovation*, 35 ADMIN. SCI. Q. 128, 128–29 (1990) (defining "absorptive capacity" as a firm's ability to recognize, assimilate, and apply new knowledge).

For example, Goldman Sachs' "elite" identity,[319] IKEA's frugality ethos,[320] and 3M's innovation rituals[321] demonstrate how long-standing narratives and practices guide decision-making well beyond any single leader's tenure, and why attempts at quick fixes often fail in the absence of engagement with these deeper layers.[322]

4.2.8. Other Enabling Mechanisms of Internal Cultural Change

Culture changes are also often shaped and sustained by less visible internal mechanisms that transmit, reinforce, or legitimize evolving norms. Among these, three examples are: internal communication and storytelling, human resources systems, and organizational slack.

First, internal storytelling plays a central role in reshaping shared values and legitimizing change. While internal narratives, artifacts, and symbols are integral elements of a company's existing culture,[323] they can also act as tools for cultural change. In this context, storytelling is not treated as culture itself, but rather as a mechanism through which culture is interpreted, reinforced, or contested.[324] When leaders, HR teams, or employees mobilize new metaphors, success stories, or symbolic rituals, they engage in a process of reshaping shared meanings.

Additionally, although internal storytelling is often initiated or encouraged by top management, through speeches, onboarding materials, or curated internal communications, for example, it is more than a top-down communication tool. It functions as a social process through which employees make sense of organizational changes, construct shared identities, and negotiate

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[319] *See* Cohan, *supra* note 236.

[320] *See* Prarthana Prakash, *How Ikea Rewrote the Rules with Inflation-Defying Prices and One of the World's Most Popular Publications*, Fortune (Apr. 30, 2025), https://fortune.com/europe/2025/04/30/ikea-furniture-frugality-creativity-inflation-ingka-kamprad/ (last visited July 31, 2025) (noting that IKEA owes much of its identity to a "relentless focus on frugality" rooted in founder Kamprad's philosophy).

[321] *See* 3M, *3M's 15% Culture*, 3M Career Website (2025), https://www.3m.co.uk/3M/en_GB/careers/culture/15-percent-culture/ (last visited July 31, 2025) (describing how employees are encouraged to use 15% of their time on self-directed innovation projects).

[322] *See*Kotter, *supra* note 248, at 143–52.

[323] *See supra* Part 2.

[324] *See* Schein, *supra* note 78, at 26–30 (defining culture as a layered phenomenon, with artifacts as visible expressions of deeper values and assumptions).

norms over time.[325] For example, Salesforce's "Ohana" concept, originally championed by CEO Marc Benioff, evolved into a cultural framework embedded in onboarding, office design, and daily rituals, reinforcing values like trust and inclusion even outside formal compliance structures.[326] This diffusion process highlights how storytelling transcends leadership alone, influencing how middle managers and frontline employees make sense of change.[327] Moreover, storytelling can persist and shape culture even in periods of leadership turnover, suggesting it functions less as a trigger and more as a cultural infrastructure.[328] For this reason, internal storytelling is treated here not merely as a subcategory of leadership, but as a distinct and cross-cutting driver of cultural continuity and transformation.

Second, human resources systems, including recruiting, onboarding, training, and promotion, serve as core vectors of cultural transmission. They encode what the organization values (e.g., autonomy, collaboration, compliance) and who is rewarded. Netflix offers a prominent example: its "No Rules" culture is operationalized through hiring practices and performance systems that privilege individual judgment, transparency, and accountability.[329] HR processes can also institutionalize DEI goals and learning priorities, especially when aligned with leadership intent.

Third, the availability of organizational slack, such as discretionary time, resources, or experimental space, shapes a firm's capacity to engage in meaningful culture work. In companies like Google, practices such as "20% time" or innovation sandboxes have allowed employees to explore mission-aligned ideas and strengthen pro-social norms.[330] Conversely, resource-

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[325] *See* YIANNIS GABRIEL, STORYTELLING IN ORGANIZATIONS: FACTS, FICTIONS, AND FANTASIES 85–91 (2000) (describing how organizational stories construct meaning and shape shared understanding); BARBARA CZARNIAWSKA, NARRATIVES IN SOCIAL SCIENCE RESEARCH 49–53 (2004).

[326] *See* SALESFORCE, *Ohana Culture*, https://www.salesforce.com/company/careers/ohana-culture/ [https://perma.cc/H5FA-WR9R] (last visited Aug. 1, 2025).

[327] *See* Gabriel, *supra* note 325.

[328] *See* Czarniawska, *supra* note 325.

[329] *See* ERIN MEYER & REED HASTINGS, NO RULES RULES: NETFLIX AND THE CULTURE OF REINVENTION 153–59 (2020).

[330] *See* Paul Gompers et al., *Corporate Culture: Evidence from the Field*, 72 J. FIN. 229, 243–47 (2019).

constrained organizations may struggle to do more than signal values, reinforcing performative rather than substantive cultural change.

These enabling mechanisms often operate in tandem with other drivers in the taxonomy, such as leadership initiatives, incentive realignments, or crisis responses. While they may not independently trigger change, they are essential to sustaining and diffusing it throughout the organization.

4.3. External Catalysts of Culture Change

4.3.1. Legal and Regulatory Change

Legal and regulatory mandates, as well as enforcement actions, can act as sudden shocks to organizational routines, particularly when they introduce binding obligations that require immediate adaptation. They can compel firms to rapidly reevaluate internal practices and align with external expectations. Sometimes these interventions lead to real, lasting cultural change. But other times, they result in only surface-level compliance, done more to check legal boxes than to bring about meaningful change.

Recent history offers many examples. The Sarbanes-Oxley Act (2002) prompted widespread shifts toward internal controls and documentation cultures.[331] The Foreign Corrupt Practices Act (FCPA) enforcement wave in the late 2000s–2010s made many multinationals incorporate anti-bribery training, internal controls, and audit trails into daily routines, although the depth and effectiveness of these measures remain contested.[332] Environmental enforcement after

[331] *See* SARBANES–OXLEY ACT of 2002, Pub. L. No. 107-204, 116 Stat. 745 (codified as amended in scattered sections of 15 U.S.C. & 18 U.S.C.); Evelyn R. Patterson & J. Reed Smith, *The Effects of Sarbanes-Oxley on Auditing and Internal Control Strength*, 82 Acct. Rev. 427, 428–30 (2007), https://www.jstor.org/stable/30243576 (last visited July 31, 2025) (finding that SOX significantly improved internal control strength and documentation rigor in audited firms).

[332] *See* Karen E. Woody, *No Smoke and No Fire: The Rise of Internal Controls Absent Anti-Bribery Violations in FCPA Enforcement,* 38 CARDOZO L. REV. 1727, 1728 (2017), https://cardozolawreview.com/wp-content/uploads/2018/08/WOODY.38.5.2.pdf (last visited July 31, 2025) (describing how firms institutionalized internal controls and audit documentation in response to FCPA enforcement pressure); Richard A. Posthuma, *Analyzing Business Research on the Foreign Corrupt Practices Act: Clusters, Gaps and Future Directions*, 25 AM. BUS. REV. 221, 229–31 (2022), https://digitalcommons.newhaven.edu/americanbusinessreview/vol25/iss2/1/ (last visited July 31, 2025) (reviewing mixed findings on the impact and effectiveness of such compliance programs).

the BP Deepwater Horizon disaster catalyzed a "safety culture" overhaul in energy companies.[333] By contrast, some mandatory ESG disclosure pilots have produced more symbolic narratives than operational change, illustrating the distinction between formal compliance and internalized norms.[334]

Soft-law instruments, such as policy signaling or emerging industry best practices or standards, tend to have a slower effect. These mechanisms cause change by influencing overall expectations, reputational pressure, and, especially, peer benchmarking. Though slower to initiate, such processes can generate authentic cultural evolution, especially when consolidated by intensive stakeholder feedback or incremental posterior regulation. For instance, the diffusion of the Task Force on Climate-Related Financial Disclosures (TCFD), the Sustainability Accounting Standards Board (SASB), and now the International Sustainability Standards Board (ISSB) guidance has gradually normalized financially material sustainability reporting and board-level oversight across sector s, often preceding hard-law adoption.[335]

Research in sociology provides many insights into how these external pressures shape corporate culture. DiMaggio and Powell argue that organizations tend to copy the forms of culture and practices that are considered normative in the industry with the objective of securing legitimacy and reducing uncertainty.[336] This behavior is driven not only by explicit regulatory demands but also by implicit expectations and standards that have been created across the sector, leading to the convergence of some cultural forms even among otherwise disparate companies.[337] Informal social networks, as demonstrated by Granovetter's theory of embeddedness, also facilitate this diffusion of cultural practices by allowing organizations to learn from one another

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[333] *See* MARK A. COHEN, *Deepwater Horizon and the Gulf Oil Spill*, in The Oxford Handbook of Corporate Social Responsibility: Psychological and Organizational Perspectives 312, 312–32 (Abagail McWilliams et al. eds., Oxford Univ. Press 2019).

[334] *See* Benjamin J. Richardson, *Mandating Sustainability Disclosure: From Transparency to Accountability*, 62 MCGILL L.J. 371, 396–401 (2016) (discussing how mandatory sustainability disclosures often result in symbolic compliance rather than substantive changes in corporate behavior).

[335] *See* Stavros Gadinis & Silvia Fregoni*, supra note*

[336] Paul J. DiMaggio & Walter W. Powell, The Iron Cage Revisited: Institutional Isomorphism and Collective Rationality in Organizational Fields, 48 Am. Sociol. Rev. 147, 150-154 (1983).

[337] *Id.*

and to adopt behaviors that are perceived as successful or appropriate in their industry.[338] Additionally, Meyer and Rowan imply that cultural adaptations of this type are often made first and foremost in order to signal compliance and legitimacy externally, more than to initiate meaningful internal change.[339] In this way, organizations may adopt new cultural forms more as an act of symbolism to satisfy regulatory or market forces than as a deep transformation, revealing the delicate dynamic between external pressure and internal change.[340]

From an economic perspective, regulation is an important factor in molding incentives and governance structures, then promoting cultural change. Economic theorists often say that regulations not only impose external constraints but also reframe the internal cost–benefit calculation placed on firms.[341] Companies are induced to adapt to the new rules to reduce risks and avoid sanctions. This reorganization can involve updating the firm's norms, remuneration systems, and decision-making processes to make them fit into the new legal demands. Moreover, as companies adjust to new regulatory forces, these adaptations can ripple across entire industries, leading to broader patterns of cultural convergence. Tushman and Romanelli (1985) studied organizational equilibrium and showed how companies react to environmental shocks like regulations and how these reactions bring about change in corporate culture.[342]

In legal research, scholars have long been interested in how regulatory mechanisms and pressures to conform with them are central forces behind cultural change in organizations. Regulatory instruments, such as those that require governance reforms and disclosure obligations, are typically instrumental in this context. Bebchuk and Fried argue that governance reforms, especially with the goal of increasing transparency, can significantly influence the ethical orientation of firms.[343] Although their work focuses primarily on executive compensation and

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[338] Mark S. Granovetter, *Economic Action and Social Structure: The Problem of Embeddedness*, 91 AM. SOCIOL. REV. 481, 484 (1985).

[339] *See* John W. Meyer & Brian Rowan, *Institutionalized Organizations: Formal Structure as Myth and Ceremony*, 33 AM. J. SOCIOL. 95, 102 (1977).

[340] *Id.*

[341] *See, e.g.,* JEAN TIROLE, THE THEORY OF INDUSTRIAL ORGANIZATION (MIT Press 1988).

[342] *See* Tushman & Romanelli, *supra* note 245.

[343] Lucian A. Bebchuk & Jesse M. Fried, Pay Without Performance: The Unfulfilled Promise of Executive Compensation 3-5 (2004).

agency problems, it highlights how governance mechanisms shape corporate priorities and managerial behavior.[344] These reforms can introduce compliance-driven cultural change, which consequently can lead to new values and practices that align with increased legal expectations.[345] In other words, changes in corporate governance systems and processes act as a catalyst, requiring firms to question their cultural assumptions in an effort to comply with new rules.

4.3.2. Litigation Risk and Court-Driven Change

In some cases, legal liability—not regulation—serves as the primary driver of cultural transformation. Lawsuits, particularly shareholder derivative actions, securities class actions, and employment litigation, can expose governance failures, spark reputational crises, and catalyze internal reforms. This path to change often operates through board-level accountability mechanisms and judicial scrutiny, sometimes achieving what formal regulation does not. A notable example is the 2023 shareholder derivative suit against McDonald's, which alleged that directors failed to oversee the company's diversity, equity, and inclusion (DEI) initiatives, violating their fiduciary duties under the Caremark doctrine.[346] Although the Delaware Court of Chancery dismissed the claim, it acknowledged the theoretical plausibility that a board's failure to monitor "mission-critical" functions like DEI could, in some circumstances, constitute oversight failure.[347]

More broadly, litigation invoking Caremark duties, traditionally limited to financial misconduct, has increasingly extended into cultural domains such as sexual harassment, racial discrimination, and workplace safety. For example, in *Marchand v. Barnhill*, the Delaware Supreme Court allowed an oversight claim to proceed where the board of an ice cream company failed to monitor food safety risks, a culturally salient and mission-critical issue.[348] Similarly, in *In*

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[344] *Id.* at 12.

[345] *Id.*

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[347] *See See* In re McDonald's Corp. S'holder Derivative Litig., No. 2021-0324-JTL, 2023 WL 387292, at *1 (Del. Ch. Jan. 26, 2023); *See also* J. Robert Brown Jr., *McDonald's: A DEI Caremark Claim*, Race to the Bottom (Feb. 2, 2023), https://www.racetothebottom.org/rttb/mcdonalds-a-dei-caremark-claim [https://perma.cc/NVX3-DBLD].

[348] *Marchand v. Barnhill*, 212 A.3d 805, 822–23 (Del. 2019) (allowing claim to proceed based on board's failure to implement any board-level reporting system for food safety risks).

re Boeing Co. Derivative Litigation, the court refused to dismiss claims alleging that Boeing's board failed to oversee safety risks after two fatal crashes, reinforcing that board inattention to core company values can constitute breach of fiduciary duty.[349]

Even unsuccessful cases can prompt boards to strengthen internal reporting channels and adopt reforms aimed at preventing future liability. Litigation pressure may lead to proactive governance changes, especially when corporate disobedience or cultural negligence becomes legally visible.[350] In this way, court-driven change can function both as a legal correction and a cultural inflection point, reinforcing or reshaping internal norms through the threat or consequence of liability.

4.3.3. Evolving ESG Norms, Investor Stewardship, and Stakeholder Expectations

Over the past two decades, ESG has become central to how companies conceptualize long-term value and risk. This shift has been driven not only by policymakers and standard-setting bodies, but also, and mainly, by investors, civil society, and employees.[351] The result is a diffuse but powerful set of expectations that encourage cultural alignment with sustainability, diversity, and other social and environmental issues.

Institutional investors have played a particularly active role in shaping these expectations. Large asset managers such as BlackRock, State Street, and Vanguard have embraced stewardship as a fiduciary tool, urging portfolio companies to integrate ESG considerations into governance structures and corporate strategy.[352] BlackRock's CEO letters have repeatedly emphasized the importance of "purpose" and long-termism, positioning culture as essential to resilience and value

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[349] *In re Boeing Co. Derivative Litig.*, No. 2019-0907-MTZ, 2021 WL 4059934, at *28–34 (Del. Ch. Sept. 7, 2021) (finding board oversight failure plausibly alleged in connection with safety culture post-737 MAX crashes).

[350] *See* Elizabeth Pollman, *Corporate Disobedience*, 68 Duke L.J. 709, 740–46 (2019), https://scholarship.law.duke.edu/dlj/vol68/iss4/2/ [https://perma.cc/LVY2-T5FB].

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[352] *See* Madison Condon, *Externalities and the Common Owner*, 95 Wash. L. Rev. 1, 26–32 (2020) (discussing how large index funds use stewardship to promote ESG and cultural reform).

creation.[353] These letters often cite climate risk, human capital, and board diversity as key indicators of forward-looking governance, effectively pressuring companies to align internal culture with external norms.

Investor stewardship also influences corporate culture through proxy proposals, shareholder resolutions, and engagement practices.[354] For example, proposals targeting racial equity audits or board oversight of climate risks have gained traction in recent years, compelling boards to address internal dynamics that were once considered outside the purview of shareholder oversight.[355] This marks a gradual but potent cultural shift: companies increasingly frame internal values and practices, such as diversity, climate alignment, or ethical supply chains, as matters of governance subject to investor scrutiny.

Beyond investors, stakeholder expectations have expanded through global ESG frameworks such as the UN Principles for Responsible Investment (PRI), the Global Reporting Initiative (GRI), and the Task Force on Climate-Related Financial Disclosures (TCFD). These voluntary regimes shape norms around transparency, accountability, and corporate purpose, often reinforced by ratings agencies and media rankings.[356] Notably, the ISSB's sustainability disclosure standards are expected to further codify these soft norms, providing quantitative tools that can institutionalize ESG-linked cultural metrics.[357]

In short, ESG expectations, particularly when amplified by investor stewardship, function as gradual, external cultural drivers that influence not only formal structures but also how companies articulate their values, evaluate performance, and respond to reputational risk.

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[353] *See, e.g.,* Larry Fink, CEO Letter to CEOs: *A Sense of Purpose* (BlackRock, 2018), https://www.blackrock.com/corporate/investor-relations/2018-larry-fink-ceo-letter [https://perma.cc/U6N7-KDZS] (last visited July 31, 2025).

[354] *See* Lucian A. Bebchuk & Scott Hirst, *Index Funds and the Future of Corporate Governance: Theory, Evidence, and Policy*, 119 Colum. L. Rev. 2029, 2061–67 (2019) (describing how stewardship practices shape firm governance).

[355] Asaf Eckstein, Visible Stewardship, 97 Wash. L. Rev. 605, 635–39 (2022) (examining the rise of high-salience ESG proposals and their influence on board and cultural oversight).

[356] *See* Gadinis & Fregoni, *supra* note 195.

[357] *See* IFRS FOUND., *IFRS S1 and S2: Climate and Sustainability Disclosure Standards* (June 2023), https://www.ifrs.org/news-and-events/news/2023/06/issb-issues-ifrs-s1-and-ifrs-s2 [https://perma.cc/S5UZ-3P45] (last visited July 31, 2025).

4.3.4. External Gatekeepers

Auditors, legal counsel, credit rating agencies, and compliance consultants are considered institutional intermediaries between business and external expectations and can act as powerful catalysts of corporate culture change or as agents reinforcing existing norms. When these external gatekeepers impose financial or legal standards, they not only regulate behavior but also serve as agents of cultural reinforcement or change.[358] They can issue evaluations or flag risks, often guide firms in deciding what behavior is acceptable, expected, or potentially punishable.[359]

As illustrations, when an external audit flags a serious weakness in internal controls, or when a credit-rating agency issues a downgrade, companies often respond with fast changes in behavior[360] from the middle layers of management, the group most directly responsible for implementing internal controls and daily risk-management routines ("tone from the middle").[361] Prominent monitorships imposed via DOJ and SEC settlements have served as catalysts for whistleblowing norms, escalation protocols, and data-driven compliance analytics that outlive the monitorship term.[362]

These gatekeepers can impact culture both ways, gradually and suddenly. Over time, repeated interactions with external auditors or legal advisors can reinforce expectations of transparency or procedural rigor, contributing to a slow evolution in organizational norms and behavior. For example, Donald Langevoort argues that external legal actors influence corporate

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[358] *See* JOHN COFFEE, GATEKEEPERS: THE PROFESSIONS AND CORPORATE GOVERNANCE 7 (2006).

[359] *Id.*

[360] *See* Evelyn R. Patterson & J. Reed Smith, T*he Effects of Sarbanes-Oxley on Auditing and Internal Control Strength*, 82 ACCT. REV. 427, 428–30 (2007) (finding that adverse external audit findings, such as "material weaknesses," prompt significant internal changes).

[361] *See* Michael W. Peregrine, *The Importance of Tone in the Middle*, HARV. L. SCH. F. ON CORP. GOVERNANCE (Apr. 29, 2020), https://corpgov.law.harvard.edu/2020/04/29/the-importance-of-tone-in-the-middle/ (last visited July 31, 2025) (explaining that mid-level management behavior is critical to embedding cultural change).

[362] *See* Bradford C. Mank, *Compliance Monitorships: Implications for Corporate Culture and Ethics*, 18 Berkeley Bus. L.J. 233, 245–49 (2021), https://scholarship.law.berkeley.edu/bblj/vol18/iss2/3/ (last visited July 31, 2025) (analyzing how monitorships imposed in DOJ/SEC settlements serve as catalysts for long-term institutional changes in whistleblower protections, data analytics, and managerial accountability).

behavior not only through enforcement but through ongoing monitoring that ends up contributing to changing internal expectations and behavioral norms.[363]

However, gatekeepers may also initiate abrupt cultural shifts. For example, when a critical audit report or whistleblower investigation reveals severe governance deficiencies, this can result in sudden leadership changes or heightened internal and external scrutiny.[364] In this way, gatekeepers serve not only as compliance enforcers but also as cultural translators and transmitters of external standards.[365] Their influence is particularly acute in sectors where regulatory complexity or reputational risk is high, such as finance, pharmaceuticals, or tech. Importantly, gatekeepers help determine whether a firm's cultural response to legal or market pressure becomes meaningful or remains just symbolic. Therefore, they play a dual role: maintaining existing norms when firms meet expectations, and challenging those norms when problems arise.

4.3.5. Market and Competitive Dynamics

In addition to the drivers discussed earlier, market dynamics and competitive pressures are potential catalysts for corporate cultural change. Companies often reshape their internal culture in response to changing customer expectations or the need to innovate more rapidly than competitors, for example. In such cases, cultural adaptation becomes essential not only for competitiveness but also for long-term survival.

For instance, Netflix's "Freedom and Responsibility" culture supports rapid iteration and creative autonomy in a fast-moving entertainment industry.[366] Apple's culture of secrecy and design perfectionism reflects its premium market positioning, where innovation and differentiation

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[363] *See* Donald C. Langevoort, *Monitoring: The Behavioral Economics of Corporate Compliance with Law*, 2002 COLUM. BUS. L. REV. 71, 79–83.

[364] *See*, e.g.,*DWS Whistleblower Desiree Fixler Still Hasn't Received SEC Payout*, FINANCIAL NEWS LONDON (June 16, 2024), https://www.fnlondon.com/articles/dws-whistleblower-desiree-fixler-says-she-still-hasnt-got-an-sec-payout (detailing Fixler's 2021 whistleblowing on DWS's greenwashing practices and subsequent investigations following her complaint).

[365] *See* Ronald J. Gilson & Reinier H. Kraakman, *The Mechanisms of Market Efficiency*, 70 VA. L. REV. 549, 622–28 (1984) (explaining how gatekeepers such as auditors and lawyers act as reputational intermediaries, transmitting market-relevant information and shaping firm behavior in line with investor expectations).

[366] *See* ERIN MEYER & REED HASTINGS, NO RULES RULES: NETFLIX AND THE CULTURE OF REINVENTION 153–59 (2020).

are strategic imperatives.[367] Amazon's focus on frugality and customer obsession stems from its low-margin, high-scale business model and relentless competitive strategy.[368] These examples show how companies strategically adjust cultural norms to align with their positioning and market ambitions.

More broadly, market pressures, whether from intensifying competition, evolving consumer preferences, or technological disruption, can push companies to adopt cultures that emphasize agility, innovation, or efficiency.[369] In fast-changing industries like tech, firms are encouraged to cultivate norms that reward experimentation and adaptability. In cost-sensitive sectors such as airlines, transportation, or retail, cultures often evolve to emphasize thrift and operational discipline. These market pressures can change a company's culture gradually through competition or imitation of peers, but they can also change it abruptly, at moments of disruption, such as a crisis, bankruptcy or the entry of a powerful rival into the market.[370] To give another example, competitive environments often reward behaviors that align with the need for survival and growth.[371] But this can come at a price. Over time, these traits can crowd out softer cultural elements, such as collaboration or long-term thinking, if they are perceived as misaligned with competitive success.

Management scholars have recognized the link between market context and corporate culture for a long time. An important contribution comes from Tom Burns and G.M. Stalker, who

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[367] *See* ADAM LASHINSKY, INSIDE APPLE: HOW AMERICA'S MOST ADMIRED—AND SECRETIVE—COMPANY REALLY WORKS 71–76 (2012).

[368] *See Leadership Principles*, *Amazon Jobs*, AMAZON CAREERS (last visit Aug. 3, 2025) (emphasizing "customer obsession" and "frugality" as core principles that underpin Amazon's strategy of driving growth through operational discipline and relentless customer focus).

[369] *See* Dulce Gonçalves, Magnus Bergquist, & Richard Bunk, *Cultural Aspects of Organizational Agility Affecting Digital Innovation*, 16 J. ENTERP. MGMT. & INNOVATION 13 (2020) (showing that organizations with Clan or Adhocracy cultural types, characterized by innovation, adaptability, and agility, outperform those with Hierarchy or Market cultures, especially in driving digital innovation under competitive pressure).

[370] *See, e.g.,* William Langewiesche, *The Human Factor*, VANITY FAIR (Sept. 17, 2014), https://www.vanityfair.com/news/business/2014/10/air-france-flight-447-crash (documenting how the 2009 crash of Flight 447 precipitated a tectonic shift in cockpit culture through the widespread adoption of CRM practices as an emergency response).

[371] *See* Jennifer Dublino, *Competition in the Workplace: 6 Things to Know*, BUSINESS.COM (May 8, 2025), https://www.business.com/articles/gal-rimon-workplace-competition/ (noting that "[a] highly competitive culture can encourage unethical behavior … when someone's job security hinges on hitting aggressive … targets, the pressure can tempt them to cut corners — or worse").

famously distinguished between "mechanistic" and "organic" systems of organization.[372] Their work demonstrated that stable, predictable environments tend to foster hierarchical, rule-based, and rigid cultural forms, what they called mechanistic systems. In contrast, dynamic markets require more decentralized and adaptive culture, called organic systems. More recently, scholars have argued that in sectors characterized by volatility or shifting stakeholder expectations, organizational culture must evolve continuously to remain viable.[373] They say that static cultural models may become "liabilities," as they limit companies' ability to respond appropriately to emerging trends.[374] Based on this, other authors emphasize the importance of cultivating "learning cultures" to support ongoing adaptation.[375]

4.3.6. Media Exposure and Public Scandals

In the contemporary information landscape, media exposure can also function as an independent and powerful driver of corporate culture change. Viral social media posts and investigative journalism, for example, have catalyzed swift and sometimes dramatic shifts in corporate behavior, often preceding regulatory or investor intervention.[376] Unlike slower-moving internal processes or traditional external gatekeepers, public scandal imposes immediate reputational pressure and stakeholder scrutiny, prompting companies to reassess internal values, as well as the tone of leadership positions and accountability mechanisms.

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[372] *See* TOM BURNS & G.M. STALKER, THE MANAGEMENT OF INNOVATION 96–102 (Tavistock Publ'ns 1961) (identifying cultural patterns that vary between stable and turbulent market environments).

[373] *See* MARY JO HATCH, ORGANIZATION THEORY: MODERN, SYMBOLIC, AND POSTMODERN PERSPECTIVES 131–35 (4th ed. 2018) (explaining how external competition and turbulence drive symbolic and adaptive cultural shifts).

[374] *See* Jennifer G. Hill, *Corporate Culture and Liability*, EUROPEAN CORPORATE GOVERNANCE INSTITUTE (ECGI) - LAW WORKING PAPER NO. 502/2020 (2020), available at https://www.ecgi.global/sites/default/files/Corporate%20Culture%20and%20Liability-%20Paper.pdf.

[375] *See* Edmondson, *supra* note 287 (exploring how fostering psychological safety within organizations can cultivate a robust learning culture, driving innovation and growth).

[376] *See* Alice Martiny, Jonathan Taglialatela, Francesco Testa & Fabio Iraldo, *Determinants of Environmental Social and Governance (ESG) Performance: A Systematic Literature Review*, J. Clean. Prod. (2024), https://doi.org/10.1016/j.jclepro.2024.140916.

High-profile media coverage of unethical or unlawful corporate behavior can bring internal cultural deficiencies to light, pressuring firms to initiate actions such as internal investigations, restructurings, or a reframe of organizational values. For example, when *The New York Times* exposed Amazon's warehouse conditions, there was a public reckoning with its labor practices and a review of its safety initiatives.[377] In another example, *The Guardian*'s reporting on forced labor in the Thai seafood industry pushed multinational companies, including Nestlé and Walmart, to reevaluate their supply chain practices and publicly commit to stronger human rights due diligence.[378]

Whistleblower revelations often gain traction precisely because they are amplified through media channels. Uber's cultural crisis in 2017 was triggered not merely by internal complaints but by the viral publication of engineer Susan Fowler's blog post detailing sexual harassment and managerial indifference.[379] The widespread public response prompted Uber to initiate an external investigation and implement a multi-year culture reset. Similarly, Frances Haugen's release of the "Facebook Papers" to *The Wall Street Journal* and Congress in 2021 intensified public and regulatory pressure on Meta to reconsider its internal values and algorithmic priorities.[380]

Academic literature increasingly recognizes the role of media and reputational intermediaries as de facto regulators of corporate conduct. "Information flow and reputational sanctions" are integral to corporate law's functioning, even when formal legal sanctions are

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[377] *See* Jodi Kantor & David Streitfeld, *Inside Amazon: Wrestling Big Ideas in a Bruising Workplace*, N.Y. TIMES (Aug. 15, 2015), https://www.nytimes.com/2015/08/16/technology/inside-amazon-wrestling-big-ideas-in-a-bruising-workplace.html [https://perma.cc/8ST7-9H38] (last visited July 31, 2025).

[378] *See* Kate Hodal, Chris Kelly & Felicity Lawrence, *Revealed: Asian Slave Labour Producing Prawns for Supermarkets in US, UK*, THE GUARDIAN (June 10, 2014), https://www.theguardian.com/global-development/2014/jun/10/supermarket-prawns-thailand-produced-slave-labour [https://perma.cc/3FRK-HSJF] (last visited July 31, 2025).

[379] *See* Fowler, *supra* note 256; Mike Isaac, *Uber's C.E.O. Resigns Under Pressure*, N.Y. TIMES (June 21, 2017), https://www.nytimes.com/2017/06/21/technology/uber-ceo-travis-kalanick.html [https://perma.cc/85WS-ZJ7S] (last visited July 31, 2025).

[380] *See* Jeff Horwitz, *Facebook Knows Instagram Is Toxic for Teen Girls, Company Documents Show*, WALL ST. J. (Sept. 14, 2021), https://www.wsj.com/articles/facebook-knows-instagram-is-toxic-for-teen-girls-company-documents-show-11631620739 [https://perma.cc/8THZ-5X4M] (last visited July 31, 2025).

absent.[381] Media attention thus does not merely expose misconduct, it shapes the internal and external expectations that drive corporate cultural adaptation.

4.3.7. Societal and Technological Changes

Expectations around ESG, transparency, and stakeholder engagement are influenced to a great extent by societal movements, such as Black Lives Matter,[382] MeToo,[383] climate activism[384] and racial equity advocacy.[385] These social movements can create mounting pressure on firms to adapt culture and change practices and are often amplified by media scrutiny, investor pressure, and demands of younger generations of employees and customers. For example, the #MeToo movement catalyzed rapid overhauls of reporting channels, investigation protocols, and leadership accountability at firms in entertainment and technology,[386] and the post-2020 racial equity focus spurred board-level oversight of DEI commitments and supplier-diversity initiatives.[387]

Although cultural adaptation in response to social change is often gradual, these movements can also create sudden inflection points, particularly when catalyzed by viral incidents that become external calls for accountability. These moments often force firms to rapidly reassess

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[381] *See* Roy Shapira, *supra* note 277. *See also* Roy Shapira, *Reputation Through Litigation: How the Legal System Shapes Behavior by Producing Information*, 91 WASH. L. REV. 1193, 1196–99 (2016), https://digitalcommons.law.uw.edu/wlr/vol91/iss3/7 [https://perma.cc/ZGR9-6BXX] (last visited July 31, 2025).

[382] *See* BLACK LIVES MATTER, *Herstory*, https://blacklivesmatter.com/herstory/ (describing the origins and goals of the Black Lives Matter movement in elevating racial justice and structural inequality issues).

[383] *See* Tarana Burke, *#MeToo Was Started for Black and Brown Girls. They're Still Being Ignored*, WASH. POST (Nov. 8, 2017), https://www.washingtonpost.com/news/post-nation/wp/2017/11/08/metoo-was-started-for-black-and-brown-girls-theyre-still-being-ignored/ (discussing the origin of the #MeToo movement and its role in changing corporate norms around sexual harassment and accountability).

[384] *See* Coral Davenport, *World's Youth Take to the Streets to Demand Climate Action*, N.Y. TIMES (Sept. 20, 2019), https://www.nytimes.com/2019/09/20/climate/global-climate-strike.html (capturing the global youth-led climate movement's impact on public pressure toward corporate environmental responsibility).

[385] *See* Alexis Ohanian, *Why I'm Stepping Down from the Reddit Board*, MEDIUM (June 5, 2020), https://medium.com/@alexisohanian/why-im-stepping-down-from-the-reddit-board-519edc78af20 (showing an example of corporate leaders taking action in response to racial equity advocacy, demonstrating its influence on corporate governance and culture).

[386] *See* Edelman, *supra* note 288.

[387] *See* Steven A. Ramirez, *Lessons from the Financial Crisis: The Case for a Culture of Compliance*, 1 Wm. & Mary Bus. L. Rev. 225, 238–42 (2010).

internal practices and value statements in order to preserve stakeholder trust or social license to operate. For example, a public backlash to a labor rights violation in a company's supply chain could trigger internal reflection and cultural change, leading to revisions in sourcing practices.[388] This happened with Nike in the face of reports of sweatshop conditions in overseas factories, which triggered broad criticism and consumer protests.[389] In response, Nike initiated internal reforms, including increased supply chain transparency, a code of conduct for suppliers, and independent monitoring.[390]

Companies that grew rapidly under Silicon Valley's disruption ethos have often needed to pivot toward stakeholder accountability due to societal and reputational pressure. For example, Airbnb, after facing widespread criticism over racial bias on its platform and safety failures,[391] adopted platform-wide anti-discrimination policies and launched a civil rights audit to increase safety systems.[392]These reforms were not mandated by regulation but emerged from public scrutiny and reputational pressure.

Broad technological changes can also contribute to changes in corporate culture. It is the case with the current artificial intelligence boom, which requires firms to adapt not only their operations but also their ethical frameworks, employee roles, and internal narratives about responsibility and risk (e.g., regarding the use of new tools). Large data platforms have developed AI ethics groups and responsible AI playbooks, embedding new decision-making norms (e.g., data

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[388] *See* David A. Skeel Jr., *Shaming in Corporate Law*, 149 U. PA. L. REV. 1811, 1814–15 (2001) (discussing reputational and social pressure as mechanisms for corporate norm enforcement).

[389] *See, e.g., Nike Fires Back at Protesters*, WIRED (June 1, 2000) (describing Nike's initiative to post factory inspection data online and allow public scrutiny).

[390] *See* NIKE, INC., *Corporate Responsibility Report FY05–06*, at 5–7 (2007), https://purpose.nike.com/reports.

[391] *See* Benjamin Edelman, *Racial Discrimination in the Sharing Economy: Evidence from a Field Experiment*, 9 AM. ECON. J.: APPLIED ECON. 1 (2017), https://www.aeaweb.org/articles?id=10.1257/app.20160213 [https://perma.cc/7DLZ-ZNKR].

[392] *See* Erin Griffith, *Airbnb to Conduct a Civil Rights Audit*, N.Y. TIMES (June 20, 2020), https://www.nytimes.com/2020/06/20/technology/airbnb-civil-rights-audit.html [https://perma.cc/B9Y7-WHYJ]; Airbnb, *Airbnb's Work to Fight Discrimination and Build Inclusion*, https://news.airbnb.com/airbnbs-work-to-fight-discrimination-and-build-inclusion/ [https://perma.cc/UGZ8-5CEK] (last visited Aug. 1, 2025). Katie Benner, *Airbnb to Verify All 7 Million Listings After Scams and Safety Concerns*, N.Y. TIMES (Nov. 6, 2019), https://www.nytimes.com/2019/11/06/technology/airbnb-verification.html [https://perma.cc/NMB2-TZUZ].

lineage, bias testing, human-in-the-loop controls) across product and compliance teams.[393] These shifts often involve new ways of thinking about accountability, data governance, privacy, and human-machine interaction, which, therefore, require corresponding changes in training, leadership style, and consequently in organizational identity.[394] Finally, the rapid diffusion of ideas through social media is increasingly seen as an outside force that drives and accelerates changes in business culture.[395]

4.3.8. Political and Economic Shifts

Political and economic shifts, such as financial crises, wars, inflationary shocks, or political regime changes, can be powerful external catalysts for cultural transformation. Clear cases include the 2008 financial crisis, which pushed banks toward risk awareness and capital discipline (with mixed cultural embedment),[396] and the COVID-19 pandemic, which normalized remote and hybrid work and forced firms to articulate trust-based performance cultures in distributed environments.[397] Similarly, geopolitical disruptions like the Russia–Ukraine war prompted multinationals to re-evaluate supply-chain ethics and localization strategies, with effects for internal risk culture.[398]

These disruptions are often sudden shocks, changing routines and risk scenarios abruptly, and prompting companies to rethink their strategies. Companies may then adjust their internal values and behaviors in response to this shock, going toward a culture of austerity, nationalism or regulatory prudence, depending on the circumstances. For example, the 2008 global financial crisis and its economic impacts and regulations led firms to adopt a culture centered on risk avoidance,

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[393] *See* Brent Mittelstadt, *Principles Alone Cannot Guarantee Ethical AI*, Nat. Mach. Intell. 501, 503–04 (2019).

[394] *See* Cary Coglianese & David Lehr, *Transparency and Algorithmic Governance*, 71 ADMIN. L. REV. 1, 4–6 (2019) (exploring how emerging technologies like AI challenge regulatory and cultural norms inside organizations).

[395] *See* Martiny, *supra* note 376.

[396] *See* Steven A. Ramirez, *Lessons from the Financial Crisis: The Case for a Culture of Compliance*, 1 Wm. & Mary Bus. L. Rev. 225, 238–42 (2010).

[397] *See* Mark Fenwick, Wulf Kaal & Erik P. M. Vermeulen, *The COVID-19 Pandemic and Corporate Culture*, *Eur. Bus. Org. L. Rev.* 157, 163–67 (2021), https://link.springer.com/article/10.1007/s40804-021-00225-2 [https://perma.cc/6KJP-4J78] (last visited July 31, 2025).

[398] *See* Cary Coglianese & David Lazer, *Management-Based Regulation: Prescribing Private Management to Achieve Public Goals*, 37 Law & Soc'y Rev. 691, 703–08 (2003).

transparency, and compliance.[399] The COVID-19 pandemic forced companies to cultivate a unified culture even with employees working from different places around the globe.[400] \

However, political and economic changes can also operate as slower, more systemic forces. Prolonged economic crises or evolving public sentiments about political norms, for example, can change corporate culture incrementally.[401] Over time, these forces can influence many aspects of companies' practices, including their hiring processes, the language they use in communications, the way they interact with consumers, and the expectations of leadership. Ultimately, the pace and depth of cultural transformation in response to political or economic change depend largely on the immediacy of the threat, the size of its impact, and the company's adaptive capacity. It is fair to conclude that companies that see their survival as threatened are more likely to adopt lasting cultural changes, while others may make only superficial adjustments.

4.4. Empirical Evidence on Catalysts of Cultural Change

After identifying the main internal and external factors that have the potential to shape cultural changes, it is important to understand what has already been empirically tested and how research shows these forces acting in practice.

Empirical research on cultural change indicates that while top–down interventions and externally driven events can be potent catalysts, the outcomes are highly nuanced and, in most cases, variable. In the case of leadership influence, for example, studies have usually shown a high correlation between managers' behavior and cultural change.[402] However, several other studies have found that such top-down interventions frequently translate into merely skin-deep or

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[399] *See* Mark J. Roe, *The Impact of the Financial Crisis on Corporate Governance*, 21 MINN. J.L. INT'L L. 97, 100–05 (2012) (explaining how the 2008 crisis led to cultural shifts in governance norms and internal risk culture).

[400] *See* AMIR N. LICHT, *Culture and Law in Corporate Governance*, in THE OXFORD HANDBOOK OF CORPORATE LAW AND GOVERNANCE 467, 482–84 (Jeffrey N. Gordon & Wolf-Georg Ringe eds., 2018) (analyzing how macro-political conditions gradually shape governance-related cultural norms).

[401] *Id.*

[402] *See* Emmanuel Ogbonna & Lloyd C. Harris, *Leadership Style, Organizational Culture and Performance: Empirical Evidence from UK Companies*, 23 INT'L J. HUM. RESOURCE MGMT. 1, 1–23 (2000) (finding a strong correlation between leadership style and observed changes in organizational culture across a large sample of UK firms).

ephemeral modifications.[403] In some cases, even when initial changes appear successful, deeply ingrained assumptions and attitudes remain largely unaltered. As soon as outside pressures dissipate, employee resistance, particularly from those who feel excluded from the change program, can undo the long-term sustainability of cultural transformation.[404] For example, a study found that transformational leadership behaviors, such as open communication, clear strategic direction, and genuine participation, are strongly related to effective new cultural norm adoption in corporations, with improvements in employee engagement and satisfaction.[405] Additional research demonstrated that the leadership effect on cultural change is typically moderated by factors like employee participation and the quality of internal communication channels.[406]

Cross-case evidence mirrors these findings. Following Wells Fargo's scandal, leadership turnover and revamped controls produced formal changes, yet independent exams repeatedly questioned whether frontline norms had fully realigned.[407] Microsoft's multi-year transformation, by contrast, shows how consistent leader behaviors and symbolic actions (e.g., storytelling around growth mindset) can help entrench new norms.[408] Acquisitions like Disney–Pixar and Amazon–Whole Foods suggest that the integration design of the transactions (preserve vs. impose) affects whether cultural change sticks.[409] In regulation, SOX and FCPA enforcement waves demonstrate

[403] *See* Heskett & Kotter, *supra* note 9.

[404] *See, e.g.,* Michael Beer, Russell A. Eisenstat & Bert Spector, *Why Change Programs Don't Produce Change*, HARV. BUS. REV., Nov.–Dec. 1990, at 158, 158–66 (finding that many top–down initiatives yield only superficial, short-lived results).

[405] *See* Florensya Pamara & Emanuel Michael, *Transformational Leadership and Organizational Culture Towards Employee Engagement with Job Satisfaction as Intervening Variable*, 1 J. RES. SOC. SCI. ECON. MGMT. 12 (2022), https://doi.org/10.59141/jrssem.v1i12.222.

[406] *See, e.g.,* Cen April Yue, Linjuan Rita Men, & Mary Ann Ferguson, *Bridging Transformational Leadership, Transparent Communication, and Employee Openness to Change: The Mediating Role of Trust*, 45 PUBLIC RELATIONS REV. 101779 (2019), https://doi.org/10.1016/j.pubrev.2019.04.012.

[407] *See* JAMES E. MCNULTY & AIGBE AKHIGBE, CORPORATE CULTURE AND BANK FINANCIAL PERFORMANCE: A CASE STUDY OF THE WELLS FARGO SALES PRACTICES SCANDAl (2025).

[408] *See* Charles A. O'Reilly, *How Microsoft Transformed Its Culture: Five Levers for Organizational Cultural Change*, 4 Mgmt. & Bus. Rev. 41, 44–48 (2024).

[409] *See* Boris Groysberg & Michael Slind, *Disney–Pixar: Preserving the Magic*, Harv. Bus. Sch. Case 9-709-462 (2009); Dennis Campbell et al., *Whole Foods Under Amazon*, Harv. Bus. Sch. Case 118-074 (rev. July 2018).

that hard-law shocks can alter routines quickly, but durable internalization depends on middle-manager buy-in and incentive coherence.[410]

M&As present another empirical setting to study the challenges of cultural change. Although most of the literature focuses on how existing culture influences the success of deals, there is also evidence of the effect that M&A may have on cultural change. During a deal, corporations need to reconcile competing values and practices, providing a unique environment for transformation. For example, Haspeslagh and Jemison highlighted this situation by noting that successful post-merger integration depends on deliberately creating a new, unified culture than just accommodating old habits—demonstrating the potential for M&As to change corporate culture.[411] Similarly, M&A often trigger profound shifts in internal norms as companies seek to establish a coherent identity.[412] In this manner, while culture certainly contributes to the success of M&A transactions, aspects of corporate culture are also determined by integration itself, hence indicating a twofold relationship that demand further empirical investigations.[413]

Research based on defined temporal events that may change organizations, including leadership shifts and DEI initiative, shows nuanced results. For example, bringing in a new CEO is considered a unique event or shock that often prompts a reevaluation of the cultural norms, since new leaders are likely to have distinct management styles and strategic priorities. Yet the duration and magnitude of such changes are extremely variable, with some studies defining the effect to be dependent on the degree of existing cultural momentum and employee buy-in.[414] Similarly, while DEI interventions have been empirically linked with successful cultural adaptation, their impact is highly dependent on its design and implementation as well as the organizational context. In some

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[410] *See* Karen E. Woody, *No Smoke and No Fire: The Rise of Internal Controls Absent Anti-Bribery Violations in FCPA Enforcement*, 38 Cardozo L. Rev**.** 1727, 1728 (2017).

[411] PAUL C. HASPESLAGH & DAVID B. JEMISON, MANAGING ACQUISITIONS: CREATING VALUE THROUGH CORPORATE RENEWAL (Jossey-Bass 1991).

[412] *Id.*

[413] *See* Silvia Fregoni, *Can ESG Culture Be Acquired? The Impact of M&A on Sustainability Practices and Market Perceptions* (unpublished manuscript) (on file with author).

[414] *See,* Bernard M. Bass & Bruce J. Avolio, *Transformational Leadership and Organizational Culture*, 6 PUB. ADMIN. Q. 112, 112–17 (1993).

cases, DEI policies lead to important improvements in culture; in others, the impact seems minimal, pointing to potential gaps in understanding the mechanisms that drive such change.[415]

Moreover, it is well recognized that external forces such as regulatory mandates and shifting public sentiment make companies change their culture. But empirical findings in this area are mixed too. Some research says that while companies adopt new norms to cope with regulatory or market pressures, many times these changes do not become a part of culture and revert once outside pressures ease off. For example, Christensen & Raynor examined the effect of mandating sustainability reporting and discovered that companies initially made broad cultural shifts when confronted with new regulatory or standards demands.[416] These shifts included adopting greater transparency in communication about environmental activities and restructuring in-house procedures.[417] However, the same research supplemented that when the regulatory pressure decreased, some of these companies gradually returned to their old practices, meaning that these cultural shifts were not deeply ingrained but temporarily enforced under the pressure of the external mandates.[418] Similarly, Reinhardt et al. show that firms often pursue CSR measures only in response to market or social pressure.[419] Therefore, if these types of changes may initially seem substantial, they are often shelved if external pressures ease or stakeholders' demands shift. Illustratively, post-2008 banking reforms formalized risk and compliance routines but often struggled to shift sales practices and informal incentives.[420] Similarly, early ESG disclosure

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[415] *See* Mary Johnson, *The Role of Leadership Training in Public Sector Cultural Renewal*, 46 LEADERSHIP & ORG. DEV. J. 145 (2006).

[416] *See* Hans B. Christensen, Luzi Hail & Christian Leuz, *Mandatory CSR and Sustainability Reporting: Economic Analysis and Literature Review*, 26 REV. ACCOUNTING STUD. 1176, 1185–86 (2021)

[417] *Id.*

[418] *Id.*

[419] *See* Forest L. Reinhardt, Robert N. Stavins & Richard H.K. Vietor, *Corporate Social Responsibility Through an Economic Lens*, 26 REV. ENV'T ECON. & POL'Y 219 (2008).

[420] *See, e.g.,* Steven A. Ramirez, *Lessons from the Financial Crisis: The Case for a Culture of Compliance*, 1 Wm. & Mary Bus. L. Rev. 225, 238–42 (2010), https://scholarship.law.wm.edu/wmblr/vol1/iss2/2/ [https://perma.cc/Q94C-3Y8N] (last visited July 31, 2025) (arguing that while post-crisis reforms improved formal compliance systems, many firms failed to transform core cultural incentives driving misconduct); Benjamin M. Blau et al., *Does the Dodd–Frank Act Reduce Financial Firms' Risk-Taking?*, 47 J. Corp. Fin. 1, 3–5 (2017), https://doi.org/10.1016/j.jcorpfin.2017.09.004 [https://perma.cc/J4H7-YDL9] (last visited July 31, 2025) (finding limited changes in behavior despite increased regulation).

initiatives spurred narrative and governance changes, yet in some firms these remained largely symbolic until reinforced by investor stewardship or binding regulation.[421]

5. Directions for Future Research

Given the critical role of corporate culture in the functioning of companies and the still limited number of studies on what makes it change and evolve, as well as inconclusive results in many of them, this remains an important avenue for future research. As this paper demonstrated, corporate culture operates at the intersection of economics, management, psychology, sociology and law, so scholars need to integrate insights across different fields when structuring new studies. They should also explore new theoretical frameworks as well as different methodologies, mainly leveraging AI-related tools.

Regarding theory, a promising conceptual lens to apply in this context is the principle of mutual constitution, which proposes that culture shapes individuals' psychological states and, in turn, individuals' psychological states shape cultural patterns.[422] This process has been studied within a broader sociocultural framework, which includes four interconnected layers: individual experiences and mindsets; everyday interactions; social institutions and structures; and the dominant ideas and beliefs that shape how people see the world.[423] In this view, nothing emerges in isolation; rather, it is continuously co-created through the interaction between individuals and their social environments, including organizations.[424]

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[421] *See*, Amir Amel-Zadeh & George Serafeim, *Why and How Investors Use ESG Information: Evidence from a Global Survey*, 74 FIN. ANALYSTS J. 87, 91–94 (2018), https://www.tandfonline.com/doi/full/10.2469/faj.v74.n3.2 [https://perma.cc/6P2F-K9L8] (last visited July 31, 2025) (finding that ESG reporting was often generic and lacked integration into firm strategy); Jean Rogers & Bob Eccles*, How to Move ESG Reporting from Talk to Action*, HARV. BUS. REV. (Mar. 22, 2021), https://hbr.org/2021/03/how-to-move-esg-reporting-from-talk-to-action [https://perma.cc/89JX-N2YD] (last visited July 31, 2025) (arguing that ESG reports often remained performative until pressured by investors or regulators).

[422] *See, e.g.,* Hazel Rose Markus & Shinobu Kitayama, *Cultures and Selves: A Cycle of Mutual Constitution*, 5 PERSPS. PSYCHOL. SCI. 420 (2010), https://doi.org/10.1177/1745691610375557.

[423] *See* Alexandra A. Michel, *The Mutual Constitution of Persons and Organizations: An Ontological Perspective on Organizational Change*, 25 ORG. SCI. 1082 (2014).

[424] *Id.*

This theory, which originated in sociology and psychology, can be used as a complementary approach to the top-down versus bottom-up framework of corporate culture. Mutual constitution talks on the interdependent relationship between individuals (or lower levels) and institutional structures (or higher levels). Therefore, it implies that influence flows not just in one direction but rather in a reciprocal process where both elements shape and reshape each other continuously. So, while top-down and bottom-up describe asymmetrical power dynamics, mutual constitution suggests interconnectedness and feedback loops.

Embracing this perspective can bridge micro-level behavior and macro-level organizational patterns. For example, research might examine how employees' daily actions collectively reinforce or alter company-wide norms, and conversely, how established cultural norms constrain or enable individual behavior. By analyzing culture as a dynamic co-creation between agents and systems, future studies can better explain how corporate culture evolves and why it varies across firms and time. Many other questions can arise here. How does feedback loop between individual actions and organizational structures lead to the emergence of new organizational values during times of crisis or transformation (e.g., during M&A or leadership changes)? Can cultural assimilation or resistance be understood as a result of the interplay between individual and institutional norms in multicultural organizations? How do ideologies in an organization (e.g., innovation, sustainability, or diversity) become incorporated in its culture through a mutual constitution process?

On another front of study, scholars can further the application of behavioral economics and decision-making models to investigate how incentives and biases shape cultural adaptation. More specifically, how do behavioral biases, such as confirmation bias, overconfidence and anchoring,[425] affect employees' willingness to embrace or resist changes in corporate culture? In what ways can incentives (financial and non-financial)[426] be designed to align employee behavior with desired

[425] *See* Justin D. Levinson & Kaiping Peng, *Valuing Cultural Differences in Behavioral Economics*, 4 ICFAI J. BEHAV. FIN. 32 (2007), https://culcog.berkeley.edu/Publications/2007BF_CulturalEconomics.pdf.

[426] *See Understanding How Behavioral Economics Influences Incentive Program Design*, ALL DIGITAL REWARDS (Oct. 13, 2021), https://alldigitalrewards.com/blog/white-paper-understanding-how-behavioral-economics-influences-incentive-program-design.

cultural changes? How does bounded rationality[427] or organizational inertia influence cultural adaptation? Additionally, researchers can further explore Lewin's Change Model to understand how organizations navigate profound transformations through phases of unfreezing, change, and refreezing.[428] This framework may be particularly useful for examining how companies stabilize new cultural values after an initial abrupt change, as in the case of shocks such as financial scandals and mergers and acquisitions.

Another theory that can be applied in this context is the attribution theory, which focuses on how people explain why things happen, especially the actions of others or themselves.[429] In a corporation, when cultural change occurs (for example, a shift toward more sustainable actions), employees try to figure out why the change is happening. They may think the cause is internal (such as a new CEO or internal leadership decisions) or external (such as new regulations or public pressure).[430] According to this theory, the way employees interpret the causes of the changes affects the way they respond to them—they may be more open or resistant to the change according to who or what they believe is behind it.

For example, in the face of the current digital transformation, employees may attribute success or failure to many factors, such as leadership capabilities, the state of the company's technology available, or the readiness of the workforce. If they attribute failure to poor leadership or poor guidance, this can demotivate them from embracing new cultural norms. If they attribute the problem to their skill gap, for example, they may be more open to learning and adapting, accepting the new norms.

Similarly, in times of crisis, such as the one triggered by the COVID-19 pandemic, employees may attribute the impacts on employment and salaries to internal factors, like leadership failures to deal with the crisis, or to external pressures, like market forces or unforeseen global

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[427] *See* Robin P. Brown, *Bounded Rationality and Organizational Learning*, 2 ORG. SC. 125 (1991), https://pubsonline.informs.org/doi/10.1287/orsc.2.1.125.

[428] *See* KURT LEWIN, FIELD THEORY IN SOCIAL SCIENCE 206 (Harper & Row 1951).

[429] *See* HEIDER, FRITZ. THE PSYCHOLOGY OF INTERPERSONAL RELATIONS (John Wiley & Sons 1958).

[430] *See, e.g.,* Mark J. Martinko & William L. Gardner*, Attributions and Leadership: A Review*, 15 LEADERSHIP Q. 757 (2004) (explain the theory in organizational context); Bernard Weiner, *An Attributional Theory of Achievement Motivation and Emotion*, 92 PSYCHOL. REV. 548 (1985).

events. If they attribute the negative effect to internal mismanagement, this can lead to a demand for cultural reforms. On the other hand, if they see the problem as a result of external market forces, they may be more inclined to accept the situation and keep the existing culture.

ESG initiatives provide another application of attribution theory. In case of failure to uphold the commitments, employees can attribute these failures to either a toxic corporate culture or external factors. Depending on how responsibility is attributed, it can drive cultural change by addressing root causes or reinforcing existing norms that excuse unethical behavior.

5.1. New Methodologies and Measurement Tools

Scholars interested in corporate culture now have an immense amount of data to work with. Information from corporate disclosures, employee reviews, companies' websites, and social media posts, for example, offers a great opportunity to analyze corporate culture change at scale. With these large and often unstructured datasets, researchers can investigate dynamics that were previously difficult to identify. Therefore, while traditional research methods like ethnography and case studies remain valuable, others should receive growing attention. Researchers can now leverage AI-related tools and machine learning algorithms to gain deeper insight into the main elements of corporate culture, as discussed below.

5.1.1. LLMs

The most promising new frontier for empirical explorations of corporate culture is the application of Large Language Models (LLMs), such as those developed by OpenAI and Anthropic, to examine the generally unstructured, large sets of data related to organizational environment. With the growing amount of publicly available information, LLMs can read and process these texts to track cultural shifts, sentiment patterns, and normative behaviors in organizations. The ability of LLMs to understand context, syntax, and semantics to a significant degree makes it possible to identify changes in corporate language over time and provide a richer perspective on how corporate culture is evolving.

For example, LLMs can analyze employee reviews to detect how workers perceive a company's corporate culture and highlight differences between these perceptions and the firm's stated values. LLMs can also examine language changes in corporate reports to detect shifts in key terms related to sustainability, innovation, or diversity, for example, offering insights into how corporate culture adapts to external pressures like regulatory requirements or societal expectations. Also, by using datasets from many sources, researchers can uncover how corporate culture changes due to the impact of leader shifts, competition pressure, or other internal and external forces.

A few studies have already applied LLMs in the corporate culture domain, showing the potential of these tools. The paper "CultureBERT: Measuring Corporate Culture With Transformer-Based Language Models" used transformer-based models to classify employee reviews and compared the performance of these tools with traditional text classification methods.[431] The results show that the language models outperform traditional approaches: they classified 17 to 30 percentage points more of the reviews in line with a human evaluator than traditional approaches of text categorization.[432] The models were made publicly available.

Another study, "How Well Do LLMs Represent Values Across Cultures? Empirical Analysis of LLM Responses Based on Hofstede Cultural Dimensions,"[433] incorporated different models with a series of advice requests based on the 5 Hofstede Cultural Dimensions[434] a quantifiable way of representing the values of a country. In every prompt, the authors employed personas representing 36 nations and, separately, languages predominantly linked to every country in order to analyze the consistency in the LLMs' cultural understanding.[435] They found that LLMs can differentiate between one side of a value and another, as well as understand that countries have differing values, but don't always uphold the values when giving advice, and fail to understand the

[431] *See* Sebastian Koch & Stefan Pasch, *CultureBERT: Measuring Corporate Culture With Transformer-Based Language Models* (Dec. 1, 2022) (unpublished manuscript), https://arxiv.org/abs/2212.00509.

[432] *Id.*

[433] *See* Julia Kharchenko, Tanya Roosta, Aman Chadha & Chirag Shah, *How Well Do LLMs Represent Values Across Cultures? Empirical Analysis of LLM Responses Based on Hofstede Cultural Dimensions* (June 21, 2024) (unpublished manuscript), https://arxiv.org/abs/2406.14805.

[434] *See* Hofstede, *supra* note 247.

[435] *See* Kharchenko et al., *supra* note 433.

need to answer differently based on different cultural values.[436] Based on these findings, they provided recommendations for training value-aligned and culturally sensitive LLMs.[437]

A recent research applied LLMs to investigate the practice of linking executive compensation to ESG performance in U.S. public companies.[438] The authors document the extent of this practice within S&P 500 firms during the 2023 proxy season and use a combination of hand coding and GPT-auditing to extract the unstructured information that details how often executives miss, meet, or exceed the financial and ESG-based targets in their compensation plans.[439] They concluded that LLMs could be of real value to supplement human examination of firms' proxy statements, though they struggled with issues such as "hallucinations," textual output that is not consistent with the true content of the document, or misclassifications.[440]

Data quality from both the models and the unstructured datasets represents one of the greatest challenges in using LLM for corporate culture studies. LLMs are highly dependent on the training data, and the data quality influences the accuracy of the insights that the models produce. If the training data is biased, incomplete, or not representative of the population, it can lead to systematic errors or misclassifications of the outcomes.[441] For example, if the training dataset contains biased language or unbalanced portrayals of various groups, the LLM can unwittingly continue those biases, resulting in distorted conclusions regarding corporate culture or organizational behavior.

Additionally, when using LLMs to analyze corporate reports or other documents, the quality of this unstructured data may be highly variable. Poorly composed or truncated text, such as reviews with vague language or ambiguous expressions, may cause LLMs to fail to recognize the correct nuances of cultural trends or misread basic organizational inclinations. Lack of context

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[436] *Id.*

[437] *Id.*

[438] *See* Badawi & Bartlett, *supra* note 183.

[439] Id

[440] Id, at 32.

[441] *See, e.g.,* Zhui Li et al., *Ethical Considerations and Fundamental Principles of Large Language Models in Medical Education: Viewpoint*, 26 J. MED. INTERNET RES., e60083 (2024), https://doi.org/10.2196/60083.(discussing privacy and data-risk concerns, and the necessity of anonymization and transparency in LLM usage).

in certain data types (e.g., employee feedback) may even cause models to overlook subtle shifts in corporate culture that cannot be quantified but are important to understand.

There are also ethical concerns in using LLMs in research, and scholars have to navigate through them carefully.[442] One of them is privacy.[443] Some business datasets, especially employee opinions and internal messages, may contain sensitive personal data or opinions. Processing and analysis of such datasets with the help of LLMs could unintentionally disclose confidential or personal data. Researchers must ensure that anonymization processes and data protection measures are in place to prevent misuse of private information. Transparency in the process of collecting data is another ethical issue. LLMs rely on massive, complex datasets that are not often publicly available, so it is difficult for external parties to view how models are trained or how data are collected. Such transparency can raise issues of accountability and bias. Also, as LLMs are trained on available datasets from various sources, like web platforms, they may end up reinforcing existing biases in society, like racial, gender, or class biases. These would be reflected in organizational studies, and discriminatory organizational practices may be reinforced unintentionally in corporate culture.

In conclusion, the potential for using LLM models is immense, but researchers must remember the potential pitfalls that they may face. The models can scale data collection and uncover cultural insights by mimicking hand-coding to extract information from non-standardized documents, a common obstacle in corporate culture studies. These tools can help track how culture changes over time and across different parts of a company, not just at one moment.

5.1.2. Integrating Multiple Methodologies

Another interesting possibility to study changes in corporate culture is to merge new AI-based methods with traditional ones, such as ethnographic studies, surveys, and field experiments.

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[442] *See* Biwei Yan et al., *On Protecting the Data Privacy of Large Language Models (LLMs) and LLM Agents: A Literature Review*, 5 HIGH-CONFIDENCE COMPUTING, no. 2, June 2025, at 100300.

[443] *Id.*

Each of them has inherent strengths that, when used together, can provide a more complete picture of how corporate culture evolves.

Surveys and ethnographic studies can provide valuable qualitative data about the employees' everyday experiences as they navigate through cultural change. Ethnography allows researchers to immerse themselves in the organizational environment and obtain detailed opinions in terms of cultural values and practices, while surveys enable them to collect large-scale quantitative information about the perceptions of the employees towards the culture and achievement of specific cultural programs. By integrating these methods with LLMs, researchers can review open-ended survey responses or employee narratives to find cultural motifs that are not necessarily apparent from data.

It would also be interesting to integrate the use of social network analysis with LLM tools. Social network analysis is used[444] to both map how norms and behavior spread through an organization and identify key agents of corporate change. This can be fed into LLMs to analyze how language, behavior, and values are transmitted and reaffirmed throughout the network. For example, by applying LLMs to social media posts or internal company emails, researchers can determine language evolution over time and use network analysis to track how these changes diffuse throughout the company and contribute to understanding top-down versus bottom-up dynamics on corporate culture. This can be especially interesting to investigate adoption or resistance to culture changes and the role of central stakeholders in shaping the values and norms of firms' culture.

The integration of multiple methodologies is crucial in augmenting causal inference and testing research findings. As social network analysis and panel data track cultural shifts diffusing and influencing organizational conduct, experimental designs and regression discontinuities, for example, can contribute to investigating the causal mechanisms behind culture change. Second, multi-method research that pairs experimental designs with text analysis allows scholars to test the

[444] *See, e.g.,* Guerrero, Laura M., & Koster, Joseph E. A., *Social Networks and the Diffusion of Organizational Culture, 34* J. APPLIED SOC. PSYCHOL. 1025 (2004); Katherine J. Klein et al., *Organizational Culture and Social Networks: A Study of Two Organizations*, 20 ORG. SCI. 347 (2009).

effectiveness of interventions in field settings and measure how these interventions affect employee perceptions as well as organizational outcomes over time.

5.2. Catalysts that Deserve Future Research

After discussing theoretical frameworks and methodologies that can be applied to research what changes corporate culture, this section identifies what are the themes that deserve more attention from scholars. I argue that the rapid rise of ESG, along with the subsequent political and stakeholder backlash, created a unique and rich environment to explore how corporate culture evolves. As companies face different ESG-related pressures from regulators, investors, employees, consumers, and society at large, they also experience internal tensions that can bring potential catalysts for transformation to the surface. The ESG landscape thus can serve as a valuable laboratory to explore the conditions under which culture changes and the mechanisms through which it does so. It also offers an opportunity to investigate the discrepancies between an organization's stated values and its actual practices, an essential step toward understanding which shifts represent genuine cultural change and which just reflect symbolic or performative adaptations.

Below, I present a list of potential catalysts of corporate culture change that deserve deeper research. While several of these catalysts can be analyzed in ESG-related contexts, they are not confined to them and can also be observed in broader organizational settings. For analytical clarity, they were divided into four broad categories: organizational events, governance and investor dynamics, external pressures, and leadership influence.

5.2.1. Organizational Events and Strategic Shifts

Strategic business events like M&As force the integration of distinct corporate cultures, raising questions about which norms prevail and how cultural alignment is achieved—or resisted. These transactions can disrupt or reaffirm existing cultural patterns, depending on power asymmetries, integration strategies, and post-merger governance, among other factors. Despite their relevance, these dynamics remain insufficiently explored in the organizational culture

literature. Similarly, going private, restructuring, or recapitalization events may reset firms' priorities, enabling or discouraging cultural renewal. While initial public offerings (IPOs) have already been studied from the perspective of culture change,[445] these other structural events remain comparatively underestimated and deserve further examination.

For example: In M&A transactions, does the culture of the acquirer dominate, or does the target's culture prevail—or is a new hybrid culture formed? How do leadership teams manage cultural integration when firms differ in their values, communication practices, or ESG agendas? Do going-private transactions entrench culture or enable strategic reorientation via culture transformation? How do recapitalizations or restructuring processes induce cultural norm changes in risk-taking, internal trust, and accountability, for instance? These questions highlight the need to understand how firms deal with these times of strategic discontinuity and whether such events are catalysts for cultural change or for the reinforcement of the existing culture.

Technological shifts and market pressures also have the potential to influence culture change, but are often underappreciated. The widespread adoption of remote work following the COVID-19 pandemic, for example, altered communication practices, hierarchical relationships, and perceptions of accountability inside the organizations. In highly competitive or innovation-driven industries, the high-speed context may force firms to change cultural norms more rapidly, especially if organizational learning or agility becomes critical to survival. So, both remote work and innovative-rich settings become fertile ground for academic investigation into how workplace norms evolve, how leadership adapts, and how culture can be maintained or transformed in increasingly decentralized and fast-changing environments. For example, in the new remote work environments, how do companies maintain cultural coherence without geographic co-location? What are the emerging norms of culture in remote work, and how do they differ from traditional ones? Does organizational culture evolve at high velocity in environments where innovation cycles are short and failure is routinized? Do firms in innovation-intensive industries develop more adaptive or experimental cultural traits, and what are the implications for long-term resilience?

[445] *See, e.g.,* Michael Ewens & Matt Marx, *Founder Replacement and Startup Performance*, 135 J. FIN. ECON. 502 (2020) (discussing how IPOs and leadership transitions affect startup culture and performance).

5.2.2. Governance and Investor Influence

As discussed earlier, corporate culture is partly influenced by corporate governance systems and processes. This poses significant questions for future studies: Does the creation of sustainability committees or the hiring of a Chief Sustainability Officer (CSO)[446] meaningfully change corporate culture? How does the composition of the board of directors affect cultural dynamics? Board diversity has been associated with risk tolerance, ethical decision-making,[447] and variations in stakeholder orientation.[448] Empirical studies also show that diverse boards are more sensitive to ESG issues.[449] There are still questions to be answered, however: Do companies with diverse boards also have more diverse cultures? Does increasing board diversity actively contribute to positive cultural evolution, or is it symbolic? This is a rich ground for further empirical research.

Apart from governance structures, different types of investors may exert distinct pressures on company behavior. Institutional investors, activist shareholders, and private equity firms can push different cultural directions, from long-term stakeholder sensitivity to short-term financial caution. A recent paper reveals how ESG-conscious investors can reconstitute internal norms, while others may stand in their way, depending on their strategic agendas.[450] Research is needed to examine not only whether certain types of investors drive cultural change, but also how competing investor influences are negotiated, particularly when ESG-focused and return-driven investors impose simultaneous, and potentially conflicting, pressures. Potential research questions in this area are: How do firms shape their culture when faced with conflicting investor mandates?

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[446] *See, e.g.,* Christoph K. Börner, *Do Chief Sustainability Officers and CSR Committees Influence CSR-Related Outcomes? A Structured Literature Review Based on Empirical-Quantitative Research Findings*, 70 J. BUS. ECON. 395 (2020).

[447] *See* Patricia M. Richard, *Board Diversity and Corporate Social Responsibility*, 38 STRATEGIC MGMT. J. 936 (2017).

[448] *See* Adel Alshammari, *Board Diversity and Stakeholder Management: The Moderating Impact of Boards' Learning Environment*, 156 J. BUS. ETHICS 759 (2019).

[449] *See* Corinne Post & Kris Byron, *Women on Boards and Firm Financial Performance: A Meta-Analysis*, 58 ACAD. MGMT. J. 1546 (2015); Gennaro Bernile, Vineet Bhagwat & Scott Yonker, Board Diversity, *Firm Risk, and Corporate Policies*, 127 J. FIN. ECON. 588 (2018).

[450] *See* Jonas Heese, Mozaffar Khan & Karthik Ramanna, *Why Don't Investors Care About ESG?,* HARV. BUS. SCH. WORKING PAPER NO. 20-084 (2022), https://www.hbs.edu/ris/Publication%20Files/20-084_fa14b895-4f71-42fa-88fd-6a5da48c8c71.pdf.

What role do investor coalitions play in defining corporate cultural priorities? And how durable are the cultural shifts initiated primarily because of investor pressure, particularly when ownership structures change over time?

5.2.3. Regulatory and Societal Pressures

External forces, particularly regulatory and social, have the potential to catalyze rapid cultural shifts. The introduction of Diversity, Equity, and Inclusion (DEI) requirements, climate disclosure mandates, or other ESG-linked policies may force firms to reevaluate internal values and operational routines. In some cases, these initiatives bring meaningful organizational change; in others, they risk becoming superficial, box-checking exercises. At the same time, the growing political backlash against ESG in certain jurisdictions creates new tensions,[451] exposing divisions within firms and challenging cultural coherence.

These fast-moving and often contradictory external signals raise important questions about the adaptability and resilience of corporate culture. Can organizational culture meaningfully evolve in response to such opposing pressures—first the rapid rise of ESG, then a forceful backlash? Or should culture remain anchored in internally consolidated values and belief systems that resist short-term swings in the external environment? To what extent do firms need to respond to fluctuating societal and regulatory expectations, and when might cultural consistency be a more effective long-term strategy than responsiveness?

Future research could also explore: How do corporations maintain internal cultural coherence while navigating polarized ESG discourse? Under what conditions do firms interpret ESG mandates as calls for genuine value alignment versus reputational risks to be managed? Do firms with stronger preexisting cultural foundations resist external pressures more effectively, or are they more vulnerable to backlash when misaligned with social trends? How do employees and

[451] *See, e.g.,* Simon Mundy, *Texas Overplays Its Hand with New Anti-ESG Law*, FIN. TIMES (Aug. 8, 2025), https://www.ft.com/content/39b97c3c-b77f-419a-8806-0653c9de4cce (criticizing Texas's new proxy advisory disclosure requirements as an overreach that could deter investor engagement and undermine shareholder empowerment).

middle managers perceive and interpret these shifts, especially when cultural signals from top leadership appear ambiguous or inconsistent?

Social media pressure amplifies cultural dynamics, with companies increasingly responding to public opinion in real time. This immediacy creates visibility, but also vulnerability, especially when a company's external communication is not supported by its internal culture. Whistleblowing and employee activism have also pointed to gaps between a company's stated values and its business practices, putting pressure on cultural alignment and greater internal accountability.[452] These developments open space for future inquirers. For example, how do firms manage cultural credibility when reputational threats come through decentralized channels such as social media or employee disclosures? What are the traits in a firm that make it likely (or unlikely) to listen to criticism emerging from its own employees or consumers through social media? How do whistleblowing and employee activism affect long-term culture evolution, particularly in firms with strong ESG narratives to the public? And how is digital transparency shifting cultural norms from the bottom up?

5.2.4. Leadership and Internal Dynamics

It is well established that leadership plays a critical role in defining, reinforcing, and transforming corporate culture.[453] The amount of time and attention that leaders direct to cultural stewardship, as famously emphasized by Bezos at Amazon and Sinegal at Costco, can have a profound impact on whether values become realized in practice or exist only superficially.[454] Research suggests that when a new CEO's values align with the company's existing culture, it often leads to stronger employee engagement and better organizational performance.[455] But when

[452] *See, e.g.,* Graham et al., *supra* note 11; Brishen Rogers, *The Social Movement Turn in Corporate Governance*, 70 WASH. & LEE L. REV. 1673 (2013). (exploring how worker and social activism influence corporate behavior).

[453] *See supra* Part 2.

[454] *See* Jennifer A. Chatman & Sandra E. Cha, *Leading by Leveraging Culture*, 29 CAL. MGMT. REV. 20 (2003) (discussing how leaders can shape culture intentionally.)

[455] *See* Charles A. O'Reilly III, David F. Caldwell, Jennifer A. Chatman & Margaret L. Doerr, *The Promise and Problems of Organizational Culture: CEO Personality, Culture, and Firm Performance*, 39 GRP. & ORG. MGMT. 595 (2014).

there is a mismatch between the leader's beliefs and the established culture, it can create friction, particularly during periods of transformation.[456] Leadership succession, especially at the CEO or upper management level, can catalyze cultural revitalization or create dysfunction when new leadership signals competing or confusing priorities.[457]

These dynamics raise some research questions for further study: Under what conditions are leaders effective agents of cultural change? To what extent can individual leaders influence deep-seated cultural norms, particularly in large or decentralized organizations? What is the role of leadership succession planning in corporate culture maintenance or development? How do leadership styles (authoritarian v. participatory, for instance) affect the durability of cultural change efforts? And are leaders' efforts more successful if they are backed by things like mission statements, performance goals, or regular communication practices? As ESG expectations become more central to the business community, how do leaders navigate cultural commitments when they are being pulled in different directions by regulators, investors, and employees? Can a leader who genuinely believes in ESG values spark real change, or does lasting impact depend more on formal systems and structures that outlive any one individual?

6. Conclusion

Corporate culture has long been recognized as a powerful force inside organizations, influencing strategy, compliance, ethical behavior, and long-term performance. Yet despite growing academic and practical interest, much of the literature continues to focus primarily on its consequences, not its sources. This paper contributes to filling this gap by making a multidisciplinary conceptual analysis of how corporate culture changes, what drives these changes, and under what conditions.

Reviewing theoretical frameworks from multiple disciplines, this paper develops a taxonomy of the catalysts that drive corporate culture transformation. It identifies a range of

[456] *Id.*

[457] *See* Thomas Hutzschenreuter, Sascha & Christoph Greger, *How New Leaders Affect Strategic Change Following a Succession Event: A Critical Review of the Literature*, 23 LEADERSHIP Q. 729 (2012).

internal and external forces that can trigger cultural change and further categorizes them into two broad types: gradual interventions, which impact culture slowly over time (e.g., governance mechanisms or incentive alignment), and sudden shocks, which prompt more immediate shifts (e.g., crises, scandals, or regulatory crackdowns). In addition, the paper clarifies what corporate culture is and is not, disentangling it from adjacent constructs such as compliance system, formal governance mechanisms, and strategic direction. This conceptual work lays the groundwork for a more structured research agenda on corporate culture: one that moves beyond vague references to values and addresses instead the specific processes and conditions under which cultural change happens.

Moving forward, research on corporate culture must go beyond theoretical framing to empirically test the drivers of cultural change and examine the mechanisms through which they present influence. This involves identifying context-specific conditions, causal pathways, and the organizational and institutional variables mediating or moderating cultural change. A promising lens in this regard is the theory of mutual constitution, which holds that individuals and culture co-evolve: culture shapes psychological states and behaviors, and in turn, individuals shape and reproduce cultural patterns. Rather than viewing culture as something handed down from leadership alone, this perspective emphasizes continuous interaction across organizational levels and external environments.

The rise of AI-based tools, especially large language models, holds huge potential to examine unstructured data such as corporate disclosures, employee opinions, and stakeholder narratives, including in social media channels, and enable deeper analysis in this area. This new technology can help scholars to trace cultural dynamics across time, units, and contexts, far beyond snapshot assessments.

As culture continues to shape the way organizations work, it is imperative to map where it comes from and how it evolves. This matters not just for researchers and business leaders, but also for regulators who set the rules and reporting standards that can encourage better, not just symbolic, corporate governance.

Part II

Corporate Sustainability Governance

1. Introduction

What is to govern a corporation in the era of climate risk, social disruption, and heightened expectations of corporate accountability? For a long part of the 20th century, corporate governance was narrowly focused on aligning managers' behavior with shareholder interests.[1] Anchored in the agent-principal theory, directors and executives were just concerned with financial oversight and return to shareholders.[2] Although American corporate law remains the same, corporations face a new world. They are also meant to measure their carbon footprint, protect human rights in global and complex supply chains, and disclose risks once considered well out of corporate reach.[3] In short, the question of *how* a company is run now includes the question of *what* it is run for.

At the heart of this shift lies a deeper theoretical legal struggle: the conflict between shareholder primacy and stakeholder governance.[4] This topic, which has been in the spotlight in legal circles before,[5] has reemerged as the most controversial issue in corporate law today.[6] Those

[1] *See* Michael C. Jensen & William H. Meckling, *Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure*, 3 J. FIN. ECON. 305 (1976), https://doi.org/10.1016/0304-405X(76)90026-X.

[2] *See* Eugene F. Fama, *Agency Problems and the Theory of the Firm*, 88 J. POL. ECON. 288, 290 (1980), https://www.jstor.org/stable/1837292.

[3] *See, e.g.,* WORLD ECON. F., *Global Risks Report 2025* (Jan. 15, 2025), https://www.weforum.org/reports/global-risks-report-2025 (noting that environmental, social, geopolitics and technological risks are increasingly interlinked, with climate change, supply chain fragility, and human rights concerns ranking among the top emerging business threats).

[4] Leo E. Strine Jr., *Toward Fair and Sustainable Capitalism*, 76 BUS. LAW. 363 (2021–2022). https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3680920.

[5] *See* Dorothy S. Lund, *Toward a Dynamic View of Corporate Purpose* (EUR. CORP. GOVERNANCE INST., Law Working Paper No. 746/2023, 2023), https://ssrn.com/abstract=4665040.

[6] *See, e.g.,* Lucian Bebchuk & Roberto Tallarita, The Illusory Promise of Stakeholder Governance, 106 Cornell L. Rev. 91 (2020), https://scholarship.law.cornell.edu/clr/vol106/iss1/3.

who advocate shareholder primacy consider that companies must keep the focus on maximizing shareholder value,[7] while critics argue that firms have obligations to a broader group of stakeholders.[8] These tensions raise fundamental questions about corporate purpose, and, by implication, about the governance structures required to enable it.[9] However, this debate often obscures, or mistakenly relegates to the background, the reality that significant changes in corporate governance are already underway.

Recent scholarship has begun to recognize this shift, particularly in the context of corporate climate governance.[10] As one recent study has made clear, climate disclosure regulations, such as those adopted by the European Union, the U.S. Securities and Exchange Commission and California, have started to formalize the oversight of climate-related risk within corporate governance systems.[11] Although these regimes are not about corporate governance, they have brought real changes for corporations.

This paper build on this work but goes further. It argues that what we are witnessing is not only the rise of climate governance, but instead the emergence of a wider comprehensive system: *corporate sustainability governance*. This governance paradigm inscribes environmental and social factors, spanning carbon footprint and biodiversity loss to human rights due diligence and labor conditions. Also, this paper argues that this transformation is not only being driven by regulation. Corporate voluntary commitments, along with reporting under standards like the Global Reporting Initiative (GRI),[12] the Task Force on Climate-related Financial Disclosures

[7] *See, e.g.,* Stephen M. Bainbridge, In Defense of the Shareholder Wealth Maximization Norm: A Reply To Professor Green, 50 *Wash. & Lee L. Rev.* 1423 (1993), https://scholarlycommons.law.wlu.edu/wlulr/vol50/iss4/5.

[8] *See* Margaret Blair & Lynn Stout, *A Team Production Theory of Corporate Law*, 85 VA. L. REV. 247 (1999), https://doi.org/10.2307/1073662.

[9] *See* Edward B. Rock, *For Whom Is the Corporation Managed in 2020?: The Debate Over Corporate Purpose*, 76 *BUS. LAW.* 363 (2021), https://scholarship.law.upenn.edu/faculty_scholarship/2198.

[10] *See* Virginia Harper Ho, *Corporate Climate Governance*, ECGI WORKING PAPER NO. 719/2024 (2024), https://ssrn.com/abstract=4742083.

[11] *Id*.

[12] *See* GLOB. REPORTING INITIATIVE, *GRI Standards* (2021), https://www.globalreporting.org/standards/ (last visited Mar. 10, 2025)

(TCFD)[13] and the GHG Protocol,[14] have brought changes to governance structure and processes. Both regulatory and voluntary initiatives are defining how sustainability is mainstreamed into corporate governance.

Another key argument of this paper is that corporate sustainability governance is a structural shift in the architecture of corporate governance. It does not displace traditional models of shareholder primacy or principal-agent theory, but expands their reach, both theoretically and practically. Companies are already adopting new governance tools: board sustainability committees, ESG-linked compensation, internal controls over sustainability data, and disclosure systems in line with evolving global standards and practices. In most cases, such mechanisms are adopted not through legal necessity but due to market and peers' pressure, reputation concerns, and shareholder expectations. Sustainability governance is, therefore, a hybrid regime: one that erases the boundary between voluntarism and compliance, between soft law and legal obligation.[15]

The paper also argues that as the new governance practices become institutionalized, they will not be so readily dismantled, even during a period of political backlash or rhetorical turbulence.[16] Moreover, even with the U.S. federal climate disclosure mandate overturned,[17] the underlying governance structures it helped promote are unlikely to be completely dissolved. State-level legislation may help fill existing regulatory gaps,[18] and the broader trend toward global convergence on sustainability standards ensures that companies will continue to face pressure to

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[13] *See* TASK FORCE ON CLIMATE-RELATED FINANCIAL DISCLOSURES, *Recommendations of the Task Force on Climate-related Financial Disclosures* (2017), https://assets.bbhub.io/company/sites/60/2021/10/FINAL-2017-TCFD-Report.pdf.

[14] *See* WORLD RES. INST. & WORLD BUS. COUNCIL FOR SUSTAINABLE DEV., *Standards & Guidance, GHG Protocol*, https://ghgprotocol.org/standards-guidance (last visited Feb. 4, 2025) (noting that more than 9 out of 10 Fortune 500 companies that provide emissions reporting use the GHG Protocol).

[15] *See* Gunther Teubner, *Substantive and Reflexive Elements in Modern Law*, 17 LAW & SOC'Y REV. 239 (1983), https://www.jstor.org/stable/3053348 (explaining reflexive law as a regulatory approach that promotes self-regulation through procedural obligations, such as disclosure and internal oversight, rather than imposing substantive rules).

[16] *See, e.g.,* Greg Iacurci, *'Game Over' for ESG Investing Due to Trump Backlash? Analysts Say No*, CNBC (Mar. 31, 2025), https://www.cnbc.com/2025/03/31/trumps-backlash-isnt-game-over-for-esg-investing.html.

[17] *See* U.S. SEC. & EXCH. COMM'N, *SEC Votes to End Defense of Climate Disclosure Rules* (Mar. 27, 2025) (press release), https://www.sec.gov/newsroom/press-releases/2025-58.

[18] *See*, e.g. Aliza R. Cinamon & Hilary Finkelstein, *State Climate Disclosure Bills – A Growing Trend?*, REGULATORY & COMPLIANCE (Apr. 10, 2025), https://www.regulatoryandcompliance.com/2025/04/state-climate-disclosure-bills-a-growing-trend/ (last visited May 10, 2025).

maintain robust oversight, disclosure, and accountability mechanisms, reinforced by peer benchmarking and competitive dynamics.[19]

This study contributes to the literature on corporate governance and corporate law by offering a new conceptual framework to understand changes that have already happened in these areas. It also offers new insights into the debate on stakeholder interests, with potential implications for articulations of corporate purpose, board responsibilities and executive incentives.

The paper has more four parts. Part 2 overviews the origins of traditional corporate governance, grounded in agent-principal theory and shareholder primacy, and examines the present internal and external governance mechanisms that govern corporate behavior. Part 3 describes regulatory developments, including the EU's Corporate Sustainability Reporting Directive (CSRD)[20] and Corporate Sustainability Due Diligence Directive (CSDDD),[21] the International Sustainability Standards Board (ISSB) standards,[22] the Securities and Exchange Commission (SEC) climate regulation,[23] and the California climate disclosure laws,[24] all of which integrate some kind of sustainability mandate. Part 4 discusses the governance changes brought by voluntary guidelines and business pledges. Part 5 analyzes the implications of the emergence of

[19] *See generally,* Stavros Gadinis & Silvia Fregoni*, Beyond the Brussels Effect: The Surprising Rise of the International Sustainability Standards Board*, J. INT'L ECON. L. (forthcoming 2025) (manuscript on file with authors). *See also* ANU BRADFORD, THE BRUSSELS EFFECT: HOW THE EUROPEAN UNION RULES THE WORLD (Oxford Univ. Press 2020).

[20] DIRECTIVE 2022/2464 OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL OF 14 DECEMBER 2022 ON CORPORATE SUSTAINABILITY REPORTING, 2022 O.J. (L 322) 15 (EU) [hereinafter CSRD].

[21] COUNCIL OF THE EU, *Corporate Sustainability Due Diligence: Council Gives Its Final Approval* (May 24, 2024), https://www.consilium.europa.eu/en/press/press-releases/2024/05/24/corporate-sustainability-due-diligence-council-gives-its-final-approval/ [hereinafter CSDDD].

[22] INT'L SUSTAINABILITY STANDARDS BD., *IFRS S1 General Requirements for Disclosure of Sustainability-related Financial Information* (June 26, 2023), https://www.ifrs.org/issued-standards/ifrs-sustainability-standards-navigator/ifrs-s1-general-requirements/; INT'L SUSTAINABILITY STANDARDS BD., *IFRS S2 Climate-related Disclosures* (June 26, 2023), https://www.ifrs.org/issued-standards/ifrs-sustainability-standards-navigator/ifrs-s2-climate-related-disclosures/.

[23] U.S. SEC. & EXCH. COMM'N, *SEC Adopts Rules to Enhance and Standardize Climate-Related Disclosures for Investors* (Mar. 6, 2024) (press release), https://www.sec.gov/newsroom/press-releases/2024-31.

[24] CLIMATE CORPORATE DATA ACCOUNTABILITY ACT, Cal. S.B. 253, 2023–2024 Reg. Sess. (Cal. 2023), https://leginfo.legislature.ca.gov/faces/billNavClient.xhtml?bill_id=202320240SB253; CLIMATE-RELATED FINANCIAL RISK ACT, Cal. S.B. 261, 2023–2024 Reg. Sess. (Cal. 2023), https://leginfo.legislature.ca.gov/faces/billNavClient.xhtml?bill_id=202320240SB261.

corporate sustainability governance and its reconciliation with the traditional regime, and Part 6 concludes.

2. The Foundations of Traditional Corporate Governance

Corporate governance is the system by which companies are directed and controlled,[25] establishing the mechanisms and processes for decision-making and accountability among corporate actors. It encompasses the relationships between a company's management, board of directors, shareholders, and other stakeholders, ensuring that corporate objectives are defined and pursued effectively.[26] The Organization for Economic Cooperation and Development (OECD) describes corporate governance as "the structure through which the objectives of the company are set, and the means of attaining those objectives and monitoring performance are determined."[27] Academic scholarship has further refined the understanding of corporate governance, particularly from a financial perspective. It has been seen as a mechanism to address how suppliers of capital to corporations ensure they receive a return on their investments, focusing on mechanisms that align managerial actions with shareholder interests.[28] It is a model designed to protect shareholder investments from the "claws" of opportunistic managers.[29]

In the United States, corporate governance receives influence from many sources, including statutory provisions, judicial interpretations, and regulatory frameworks. The Business Roundtable, which brings together business leaders from some of the most important American corporations, articulates corporate governance as a system of relationships among management,

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[25] *See* COMM. ON THE FIN. ASPECTS OF CORP. GOVERNANCE, *Report of the Committee on the Financial Aspects of Corporate Governance* 2 (1992) (Cadbury Report), https://www.ecgi.global/sites/default/files/codes/documents/cadbury.pdf (last visited July 11, 2025).

[26] *See* ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT, G20/OECD Principles of Corporate Governance 8 (2023), https://www.oecd.org.

[27] *Id*.

[28] *See* Andrei Shleifer & Robert W. Vishny, *A Survey of Corporate Governance*, 52 J. FIN. 737 (1997), https://www.jstor.org/stable/2329497.

[29] *See* John Roberts & Eric Van den Steen, *Shareholder Interests, Human Capital Investment and Corporate Governance*, STAN. GSB RESEARCH PAPER NO. 1631 (Apr. 30, 2000), https://ssrn.com/abstract=230019.

boards, shareholders, and stakeholders, placing particular emphasis on transparency and accountability.[30] Delaware corporate law, which heavily influences U.S. corporate governance as the principal state of incorporation, vests managerial authority in the board of directors under DGCL § 141(a). This provision underscores the primacy of board oversight, while courts apply judicial doctrines, such as the business judgment rule, to shield directors from judicial interference, provided they act in good faith, on an informed basis, and in the best interests of the corporation.[31] Through these various perspectives, corporate governance functions as a foundational system that balances power within corporations, mitigating agency problems[32] while ensuring long-term value creation.

2.1. Shareholder Primacy and the Principal-Agent Theory

Current corporate governance is largely built on the principal-agent theory, which helps explain how control and managerial accountability work in organizations.[33] This theory has roots in classical economics, but was formally developed in the 20th century, as corporations became bigger and more complex.[34] At its core, it deals with a common dilemma: when one party—the principal—relies on another—the agent—to act on their behalf, there is always a risk that their interests will not fully align.[35] In the corporate world, shareholders are the principals, and they delegate the task of running the company to managers, who act as their agents.[36] This separation

[30] *See* BUSINESS ROUNDTABLE, *Principles of Corporate Governance* 3 (Aug. 2016), https://s3.amazonaws.com/brt.org/Principles-of-Corporate-Governance-2016.pdf (last visited Mar. 20, 2025).

[31] *See* 8 Del. C. § 141(a) (2024), https://delcode.delaware.gov.

[32] *See infra* Part 2.1.

[33] *See* Eugene F. Fama, *Agency Problems and the Theory of the Firm*, 88 J. POL. ECON. 288, 290 (1980), https://www.jstor.org/stable/1837292.

[34] *See* ADOLF A. BERLE & GARDINER C. MEANS, THE MODERN CORPORATION AND PRIVATE PROPERTY (Macmillan 1932) (providing a foundational analysis of the separation of ownership and control, and explaining how the rise of large, publicly held corporations reshaped corporate governance by concentrating economic power in the hands of managers rather than dispersed shareholders).

[35] *See* Jensen & Meckling, *supra* note 1 (introducing the agency cost theory in corporate governance, explaining how the separation of ownership and control creates incentives for managers to act in their own interest).

[36] *Id.* at 310 (analyzing the shareholder–manager relationship as a principal–agent problem, in which shareholders delegate decision-making authority to managers whose objectives may not align with maximizing shareholder value).

of ownership and control creates incentives for managerial opportunism, when executives focus more on their own interests, such as compensation, status, or job security, rather than maximizing value for shareholders.[37]

This challenge has been recognized for a long time. Adam Smith (1776) observed that managers had much less incentive to carefully oversee business operations in joint-stock companies compared to the owners of the firms.[38] Berle and Means (1932) then expanded on this idea by showing how the dispersion of share ownership in large corporations weakened shareholder control, which, in turn, gives managers significant autonomy.[39] According to them, this characteristic makes corporate governance necessary to mitigate agency costs, which are the costs that arise from the need to ensure that agents act in the best interests of principals..[40] In the 1970s, Jensen and Meckling (1976) formally defined agency costs in corporate governance and proposed mechanisms to align managerial interests with shareholder value,[41] including incentive-based executive compensation, monitoring by independent directors, and shareholder activism. These elements continue to be key to corporate governance today.[42]

As a way to respond to the principal-agent problem, corporate governance was designed to give priority to shareholders interests, creating the shareholder primacy concept.[43] This governance model holds that shareholders bear the greatest financial risk—as they are the residual claimants who receive payment only after all other obligations are met—and, therefore, they should have the

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[37] *Id.* at 312 (observing that without effective governance mechanisms, managers may engage in self-serving behavior, such as excessive perquisite consumption or risk aversion, that can reduce firm values).

[38] *See generally,* ADAM SMITH, *AN INQUIRY INTO THE NATURE AND CAUSES OF THE WEALTH OF NATIONS* (R.H. Campbell & A.S. Skinner eds., Oxford Univ. Press 1976) (1776).

[39] *See* Berle & Means, *supra* note 34, at 67.

[40] *Id.* at 70 (arguing that dispersed ownership in large public corporations weakens direct shareholder oversight, thereby increasing managerial discretion and the potential for agency costs).

[41] *See* Jensen & Meckling, *supra* note 1, at 315 (presenting agency cost theory as a framework to understand conflicts between shareholders and managers, particularly in the allocation of corporate resources).

[42] *Id.* at 318 (discussing how external governance mechanisms, such as shareholder activism, hostile takeovers, and market competition, can operate to reduce agency costs and align managerial incentives with shareholder interests).

[43] *See* Lynn A. Stout, *The Shareholder Value Myt*h, 23 STAN. L. & POL'Y REV. 101, 103 (2012), https://ssrn.com/abstract=2277141 (analyzing the connection between agency theory and the shareholder primacy model, and warning that excessive focus on shareholder value may undermine long-term corporate health).

greatest governance rights.[44] While early corporate law recognized multiple corporate purposes, such as those related to broader society interests,[45] the late 20th century saw an increasing focus on shareholder wealth maximization as the mainly objective of corporate governance.[46]

The most influential articulation of shareholder primacy, that have influenced economics and corporate law since them, came from Milton Friedman (1970), who famously argued that "there is one and only one social responsibility of business: to use its resources and engage in activities designed to increase its profits so long as it stays within the rules of the game."[47] He also argued that directors and executives must prioritize shareholder returns to ensure corporate efficiency and economic growth.[48] This foundation was then developed by other scholars in law and economics. Easterbrook and Fischel (1991), for example, emphasized that shareholder primacy aligns managerial incentives with firm performance, making it the most efficient governance structure.[49] Hansmann and Kraakman (2001) stated that shareholder primacy has become the dominant corporate governance model worldwide because it best minimizes agency costs and increases firm efficiency across different legal systems.[50]

Delaware courts, in particular, have developed judicial doctrines, such as the entire fairness standard, to prevent self-dealing transactions and conflicts of interest.[51] They have also affirmed directors' primary fiduciary duty to shareholders, based on corporate law principles rather than

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[44] *See* Frank H. Easterbrook & Daniel R. Fischel, The Economic Structure of Corporate Law 9–11 (Harvard University Press 1991) (explaining how corporate law's default rules, fiduciary duties, and governance structures are designed to minimize agency costs and enhance efficient capital allocation).

[45] *See* Lund, *supra* note 5 (describing the pendulum shift in corporate governance from shareholder primacy toward stakeholder-oriented models in response to evolving social and regulatory expectations).

[46] *See* Stout, *supra* note 43 (criticizing the dominance of shareholder primacy in corporate governance discourse and advocating for alternative models that balance stakeholder interests).

[47] *See* Milton Friedman, *The Social Responsibility of Business Is to Increase Its Profits*, *N.Y. TIMES MAG.* (Sept. 13, 1970) (articulating the classical economic argument that a corporation's sole social responsibility is to maximize shareholder wealth within the bounds of the law).

[48] *Id.* (arguing that prioritizing shareholder value ensures economic efficiency).

[49] *See* Easterbrook & Fischel, *supra* note 44, at 45.

[50] *See* Henry Hansmann & Reinier Kraakman, *The End of History for Corporate Law*, 89 GEO. L.J. 439, 441 (2001), https://openyls.law.yale.edu/bitstream/handle/20.500.13051/4602/89GeoLJ439.pdf .

[51] *See Weinberger v. UOP, Inc.*, 457 A.2d 701, 710–11 (Del. 1983) (establishing the "entire fairness" standard as the appropriate standard of review in transactions involving self-dealing by a controlling shareholder or conflicted fiduciary, requiring both fair dealing and fair price).

just economic efficiency.[52] Landmark cases such as *Revlon* and *Paramount v. QVC* are critical in reinforcing the obligation of directors to prioritize shareholder value, particularly in transactions involving a change of corporate control.[53] Therefore, the principal-agent theory and shareholder primacy together form the foundation of American corporate governance. The principal-agent problem justifies the need for governance structures that ensure managerial accountability, while shareholder primacy provides the normative rationale for why corporate power should be exercised in favor of shareholders.[54] Modern corporate governance mechanisms, including board oversight, executive compensation structures, proxy voting rights, and market-based disciplinary mechanisms, are designed to mitigate agency costs and align managerial decision-making with shareholder interests.[55]

2.2. Internal Governance Mechanisms: Boards, Compensation, and Shareholder Rights

Corporate governance operates through and is influenced by mechanisms that can be internal and external. The internal mechanisms, which are the focus of this section, primarily involve board oversight, compliance and control systems, processes, shareholder rights, and executive compensation.

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[52] *See* Dodge v. Ford Motor Co., 170 N.W. 668, 684 (Mich. 1919) (holding that a corporation should be run "for the profit of the stockholders"). *See also* Leo E. Strine, Jr., *The Dangers of Denial: The Need for a Clear-Eyed Understanding of the Power and Accountability Structure Established by the Delaware General Corporation Law*, 50 WAKE FOREST L. REV. 765 (2015) (arguing that Delaware corporate law institutionalizes shareholder primacy by structuring corporate governance to prioritize shareholder interests and limit managerial discretion).

[53] *See Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.*, 506 A.2d 173, 182 (Del. 1986) (holding that when a sale of control is inevitable, the board's duty is to maximize shareholder value); *Paramount Commc'ns Inc. v. QVC Network Inc.*, 637 A.2d 34, 42 (Del. 1994) (reaffirming that in change-of-control transactions, the board must *See*k the highest value reasonably available for shareholders).

[54] *See* Jensen & Meckling, *supra* note 1 (providing a foundational analysis of agency costs and corporate governance). *See also* Stephen M. Bainbridge, *Director Primacy: The Means and Ends of Corporate Governance*, 97 *NORTHWESTERN U. L. REV.* 547, 550 (2003), https://ssrn.com/abstract=1615838 (discussing the balance between shareholder rights and board discretion).

[55] *See, e.g.,* Paul Gompers, Joy Ishii & Andrew Metrick, *Corporate Governance and Equity Prices*, 118 *Q.J. ECON.* 107, 115 (2003), https://ssrn.com/abstract=278920 (showing a positive correlation between strong governance and firm performance).

As discussed earlier, the board of directors serves as the central piece of corporate governance frameworks, with the ultimate responsibility for overseeing management and protecting the interests of shareholders.[56] A well-structured board typically has specialized committees, such as audit, compensation, and nominating or governance, each focused on specific aspects of governance to advise the board and enhance its effectiveness.[57] The independence of these committees is crucial. For example, audit committees composed entirely of independent directors are generally considered better positioned to provide impartial oversight and reduce potential conflicts of interest.[58] The National Association of Corporate Directors (NACD) has advocated for such practices, recommending that key committees be formed entirely of independent directors to strengthen the company's governance structure.[59]

Directors owe a duty of loyalty, which requires them to act in the best interests of the corporation, avoid conflicts of interest, and refrain from using their position for personal gain.[60] In Delaware, the influential *Caremark* case established that a board's failure to implement or monitor a reasonable information and reporting system may constitute bad faith, which in turn can amount to a breach of the directors' duty of loyalty.[61] More recent cases reflect a growing willingness by courts to hold directors accountable, particularly in instances of systemic compliance failures or

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[56] *See* Hansmann & Kraakman, *supra* note 50.

[57] *See* STEPHEN M. BAINBRIDGE, CORPORATE LAW 237–42 (3d ed., Foundation Press 2021) (discussing the role of board committees, particularly audit, compensation, and governance committees, in reducing conflicts of interest and enhancing oversight).

[58] *See* Jeffrey N. Gordon, *The Rise of Independent Directors in the United States, 1950-2005: Of Shareholder Value and Stock Market Prices*, 59 STAN. L. REV. 1465, 1472–74 (2007), https://scholarship.law.columbia.edu/faculty_scholarship/2933 (analyzing how independent board committees became a central feature of U.S. corporate governance).

[59] *See* NATIONAL ASS'N OF CORP. DIRECTORS, *Key Principles of Board Governance*, https://www.nacdonline.org (last visited Mar. 3, 2025).

[60] *See Guth v. Loft, Inc.*, 5 A.2d 503, 510 (Del. 1939) (establishing the fundamental duty of loyalty in corporate governance).

[61] *See In re Caremark Int'l Inc. Derivative Litig.*, 698 A.2d 959, 970 (Del. Ch. 1996). *See also Stone v. Ritter*, 911 A.2d 362, 370 (Del. 2006) (clarifying that failure to implement compliance mechanisms may constitute a breach of the duty of loyalty).

red flags that are ignored.[62] Delaware courts have also refined the application of Caremark duties and extended them to corporate officers, as seen in recent cases like *McDonald's* and *Segway*.[63]

In this way, companies must put in place effective internal control systems, including checks, procedures, and processes, to ensure that it is aligned with legal requirements.[64] The goal is to provide "reasonable assurance" that financial reports are reliable, the company is complying with laws and regulations, and operations are effective, for example.[65] However, it is not sufficient merely to establish controls. Directors must ensure that management has implemented them effectively and that information flows adequately throughout the organization to support informed decision-making.[66]

Executive compensation is also an important component of internal corporate governance mechanisms, as they are designed to align managerial incentives with shareholder interests.[67] One well-known intention is to lead executives to prioritize long-term firm performance over short-term personal gains.[68] Common forms of executive compensation include stock options, performance-based bonuses, restricted stock units, and long-term incentive plans.[69] Scholars have argued that compensation must be clearly tied to company performance to prevent problems of managerial entrenchment and make executives accountable.[70] Empirical studies have shown that firms with compensation plans that align executive pay with shareholder value tend to experience

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[62] *See Lebanon Cnty. Emps.' Ret. Fund v. Collis*, 287 A.3d 1160 (Del. 2022) (holding that directors' failure to over*See* legal compliance in opioid distribution could give rise to liability).

[63] *See McDonald's Corp. Stockholder Derivative Litig*., 289 A.3d 343 (Del. Ch. 2023) (expanding oversight duties to corporate officers); *Segway Inc. v. Cai*, C.A. No. 2022-1110-LWW (Del. Ch. Aug. 18, 2023).

[64] *See* Sanjai Bhagat & Brian Bolton, *Corporate Governance and Firm Performance*, 14 J. CORP. FIN. 257, 260 (2008), https://doi.org/10.1016/j.jcorpfin.2008.03.006.

[65] *Id*. at 262.

[66] *Id*. at 265.

[67] *See* Michael C. Jensen & Kevin J. Murphy, *Performance Pay and Top-Management Incentives*, 98 *J. Pol. Econ.* 225, 228 (1990), https://EconPapers.repec.org/RePEc:ucp:jpolec:v:98:y:1990:i:2:p:225-64 (empirically analyzing the relationship between CEO pay and firm performance, and arguing that incentive-aligned compensation can mitigate agency problems between managers and shareholders).

[68] *Id*. at 230.

[69] *See generally,* Adam B. Badawi & Robert Bartlett, *ESG Overperformance? Assessing the Use of ESG Targets in Executive Compensation Plans*, STANFORD L. & ECON. OLIN WORKING PAPER NO. 592 (Aug. 29, 2024), https://ssrn.com/abstract=4941016.

[70] *See* Jensen & Murphy, *supra* note 67, at 232.

higher profitability and stock performance.[71] However, excessive executive pay can become a governance issue, particularly when it is disproportionate to company performance or when "golden parachutes" and severance packages protect executives from market discipline.[72] The Dodd-Frank Act (2010) introduced say-on-pay provisions, granting shareholders the right to vote on executive compensation packages as a means of increasing accountability.[73]

Among the mechanisms of corporate governance designed to protect shareholders' interests, voting rights remain the most direct and powerful.[74] Other tools, such as proxy access, enhance shareholder influence and board accountability.[75] In contrast, takeover defenses, mechanisms adopted by boards to deter hostile takeovers, may serve to protect corporate strategy but can also restrict shareholder control.[76] Shareholders exercise their voting rights on critical matters, such as electing directors and approving significant corporate actions, thereby promoting accountability.[77] However, anti-takeover provisions raise some considerations. While they can protect the company—and, by extension, its shareholders—from coercive or undervalued bids, they may also insulate management from removal, even when a change in control would benefit shareholders.[78] Empirical studies show that firms with more anti-takeover provisions tend to

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[71] *See* Alex Edmans, Xavier Gabaix, Tomasz Sadzik & Yuliy Sannikov, *Dynamic CEO Compensation*, 134 *J. FIN. ECON.* 189, 191 (2019), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=1361797 (showing that long-term incentive plans improve firm performance).

[72] *See* LUCIAN BEBCHUK & JESSE FRIED, PAY WITHOUT PERFORMANCE: THE UNFULFILLED PROMISE OF EXECUTIVE COMPENSATION 1–3 (Harvard Univ. Press 2004) (arguing that excessive pay not linked to performance creates governance failures).

[73] *See* DODD-FRANK WALL STREET REFORM AND CONSUMER PROTECTION ACT, 15 U.S.C. § 78n-1 (2010).

[74] *See* David Yermack, *Shareholder Voting and Corporate Governance*, 2 *ANNUAL REV. FIN. ECON.* 103 (2010), https://www.annualreviews.org/doi/10.1146/annurev-financial-073009-104034 explaining that shareholders retain ultimate authority over board elections, mergers, and other key decisions, making voting rights the most direct governance mechanism).

[75] *See* Reilly S. Steel, *Proxy Access and Optimal Standardization in Corporate Governance: An Empirical Analysis*, 23 FORDHAM J. CORP. & FIN. L. 173 (2017), https://ir.lawnet.fordham.edu/jcfl/vol23/iss1/4/ (finding that proxy access enhances shareholder influence and board accountability).

[76] *See* Jonathan M. Karpoff & Michael D. Wittry, *Corporate Takeover Defenses*, ECGI WORKING PAPER SERIES IN FINANCE NO. 843/2022 (May 2023), https://www.ecgi.global/sites/default/files/working_papers/documents/corporatetakeoverdefenses.pdf (summarizing empirical research showing that takeover defenses can both protect corporate strategy and impose costs by restricting shareholder control, with effects varying by firm and over time).

[77] *Id*.

[78] *Id*.

exhibit lower stock returns, suggesting that these mechanisms may entrench management and reduce firm value.[79]

2.3. External Governance Pressures: Laws, Markets, and Investors

Corporate governance is also influenced by external mechanisms, including laws and regulations, market forces, institutional investor activism, media scrutiny, and creditor oversight. Legal and regulatory frameworks, for example, establish the foundational rules within which corporations operate. In the United States, the Securities Exchange Act of 1934 mandates public companies to disclose material financial information, with the SEC overseeing compliance.[80] The Sarbanes-Oxley Act of 2002, created in response to corporate scandals such as Enron and WorldCom,[81] increased internal controls and imposed more severe penalties for frauds in financial reporting, a measure that aimed at increasing the integrity of corporate disclosures.[82] Additionally, the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 enhanced shareholder rights and transparency and mandated "say-on-pay," allowing shareholders to vote on executive compensation.[83] Yet under legal standards, Delaware Law, the preferred place for firms incorporation, holds a crucial role in shaping corporate governance, including with its business judgment rule.[84]

Transparency through mandatory and voluntary disclosures ensures that stakeholders have access to important information. Laws and regulations require companies to provide accurate

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[79] *See* Gompers, Ishii & Metrick, *supra* note 55, at 132.

[80] *See* SECURITIES EXCHANGE ACT OF 1934, 15 U.S.C. §§ 78a–78qq (2024).

[81] *See, e.g.,* *THE ECONOMIST*, *Smelly Old SOX* (July 26, 2007), https://www.economist.com/leaders/2007/07/26/smelly-old-sox; David A. Lacey, *Assessing the Deterrent Effect of the Sarbanes–Oxley Act's Section 906*, VANDERBILT J. TRANSNAT'L L. (2005), https://scholarship.law.vanderbilt.edu/cgi/viewcontent.cgi?article=1527&context=vjtl (noting that the Act was widely viewed as a legislative response to perceived excesses in corporate America reflected in the Enron, WorldCom, Tyco, and Global Crossing cases).

[82] *See* SARBANES-OXLEY ACT OF 2002, Pub. L. No. 107-204, 116 Stat. 745 (2002).

[83] *See* DODD-FRANK WALL STREET REFORM AND CONSUMER PROTECTION ACT, Pub. L. No. 111-203, 124 Stat. 1376 (2010).

[84] *See supra* Part 1. *See also* DEL. CODE ANN. TIT. 8, § 141(a) (2023); *Aronson v. Lewis*, 473 A.2d 805, 812 (DEL. 1984).

financial and operational information, facilitating informed decision-making by investors and regulators.[85] But many firms go beyond legal requirements, offering additional information on corporate initiatives and governance policies to build trust and enhance credibility.[86]

Market forces act as external governance mechanisms by incentivizing companies to maintain robust governance practices. Investors usually demand transparency and accountability, so companies with poor governance may face lower valuations and higher capital costs.[87] Market forces such as the threat of takeovers can motivate underperforming management teams to improve efficiency and align with shareholder interests.[88] Moreover, companies in competitive industries are compelled to adopt efficient governance structures to remain viable and survive, as weak governance can lead to resource misallocation.[89]

The influence of institutional investors has grown, making them key external players impacting corporate governance. Large asset managers, such as BlackRock, State Street, and Vanguard, which control on average between 15% and 30% of publicly traded companies in the U.S.,[90] engage with companies on issues like board diversity and executive compensation in order to push for long-term value creation.[91] Institutional investors also utilize their voting rights to influence corporate decisions, including director elections and executive compensation.[92]

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[85] *See* 15 U.S.C. §§ 78a–78qq.

[86] *See* Christian Leuz & Robert E. Verrecchia, *The Economic Consequences of Increased Disclosure*, 38 J. ACCT. RES. 91 (2000), https://www.jstor.org/stable/2672910 (finding that firms with higher disclosure levels enjoy lower costs of capital and improved stock liquidity. It shows that both mandatory and voluntary disclosures enhance investor confidence by reducing uncertainty and fostering market trust.)

[87] *See* Gompers, Ishii & Metrick, *supra* note 55.

[88] *See* Bhagat & Bolton, *supra* note 64.

[89] *See* Lucian Bebchuk, Alma Cohen & Allen Ferrell, What Matters in Corporate Governance?, 22 Rev. Fin. Stud. 783, 790 (2009).

[90] *See* Lucian A. Bebchuk & Scott Hirst, *Index Funds and the Future of Corporate Governance: Theory, Evidence, and Policy*, 119 COLUM. L. REV. 2029 (2019), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3282794 (last visited Mar. 3, 2025).

[91] *See, e.g.,* Letter from Larry Fink, CEO, BlackRock, to CEOs, *A Sense of Purpose*, BLACKROCK (2018), https://www.blackrock.com/corporate/investor-relations/2018-larry-fink-ceo-letter; Adriana De La Cruz, Alejandra Medina & Yung Tang, *Owners of the World's Listed Companies*, OECD CAPITAL MARKET SERIES (Organisation for Economic Co-operation & Dev. 2019), https://www.oecd.org/corporate/Owners-of-the-Worlds-Listed-Companies.pdf (last visited Mar. 3, 2025).

[92] *See* Jill E. Fisch, Asaf Hamdani & Steven Davidoff Solomon, *The New Titans of Wall Street: A Theoretical Framework for Passive Investors*, 168 U. PA. L. REV. 17, 34–39 (2019), https://doi.org/10.2139/ssrn.3192069

Media outlets and public sentiment can also significantly impact corporate governance. Negative media coverage can lead to shareholder activism, consumer or employee backlash, and regulatory scrutiny, sometimes culminating in leadership changes.[93] Public and media attention on corporate practices can also pressure companies to adopt responsible business strategies, as seen during the rise of environmental, social and governance (ESG).[94] In turn, companies' creditors and credit rating agencies can exercise external influence on corporate governance by monitoring the financial health of the business.[95] More specifically, creditors often impose covenants to limit companies from taking too much risk, ensuring adherence to what is considered good governance practices.[96] Credit agencies assess governance quality as part of their evaluations and reports, broadly influencing a company's borrowing costs and access to capital. In summary, external governance mechanisms are essential in shaping corporate behavior, ensuring accountability, and aligning corporate actions with the interests of shareholders and society at large.

2.4. Pressures Challenging the Traditional Model

Although the current model of corporate governance has been around for decades, several significant developments in recent years have challenged the traditional agency cost framework.

(describing how large institutional investors use their voting power to affect corporate decisions, including director elections and executive compensation).

[93] *See, e.g.,* Jonathan M. Karpoff, Scott Lee & Gerald S. Martin, *The Cost to Firms of Cooking the Books*, 43 J. FIN. & QUANTITATIVE ANALYSIS 581, 609–11 (2008), https://doi.org/10.1017/S0022109000004221 (finding that negative press coverage following financial misconduct can trigger shareholder lawsuits, regulatory action, and executive turnover); I.J. Alexander Dyck & Luigi Zingales, *The Corporate Governance Role of the Media*, NBER WORKING PAPER NO. 9309 (Nov. 2002), https://ssrn.com/abstract=347081 (arguing that the media can discipline corporate behavior by shaping public opinion and influencing market and regulatory responses).

[94] *See*, e.e., Chenhong Zheng, Fangshun Xiao, Cong Zeng & Sasa Yang, *A Pathway Towards Corporate Sustainability: Does Media Attention Matter?*, 10 HELIYON e34489 (2024), https://doi.org/10.1016/j.heliyon.2024.e34489 (finding that media attention significantly improves corporate ESG performance and promotes sustainable business practices).

[95] *See, e.g.,* Frederick Tung, *Do Lenders Still Monitor? Leveraged Lending and the Search for Covenants*, 47 J. CORP. L. 527 (2021), https://scholarship.law.bu.edu/faculty_scholarship/1169 (arguing that lenders continue to use covenants as governance tools to influence corporate behavior, even in the leveraged lending context); Hollis Ashbaugh-Skaife, Daniel W. Collins & Ryan LaFond, *The Effects of Corporate Governance on Firms' Credit Ratings*, 42 J. ACCT. & ECON. 203 (2006), https://doi.org/10.1016/j.jacceco.2006.02.003 (showing that stronger governance mechanisms are associated with higher credit ratings, reflecting the role of rating agencies in evaluating governance quality).

[96] *Id.*

Pressing issues such as climate change and global social inequality, coupled with governmental inefficiencies in addressing these challenges, have led to increased scrutiny of business externalities.[97] This environment has encouraged interest in governance frameworks that grant management broader discretion to pursue stakeholder interests, even when these do not directly enhance shareholder value.[98] In this arena, the growth of ESG-oriented investment strategies has intensified debate over the corporate role in tackling societal issues.[99] Investors and stakeholders increasingly expect companies to implement sustainable practices and consider the broader impact of their operations,[100] reflecting a growing recognition that corporate responsibilities extend beyond maximizing shareholder value.[101]

Market conditions have prompted these changes. Research exploring historical shifts in corporate purpose noted that external economic conditions have influenced corporate governance models.[102] The author analyzed two significant corporate purpose "moments" of flux in the U.S. history: first, in the aftermath of the 1929 stock market crash, when public and regulatory distrust of corporate executives led to greater oversight and the rise of stakeholder-oriented governance; and second, following the economic stagflation of the 1970s, when faith in market efficiency revived shareholder primacy, supported by scholars like Milton Friedman and Easterbrook & Fischel.[103] As a result, she found a strong link between the state of the American economy and the

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[97] *See* Stavros Gadinis, *Social Business Judgment* (June 6, 2025) (forthcoming in *Bus. Law.*), https://ssrn.com/abstract=5284487.

[98] *See* COLIN MAYER, *PROSPERITY: BETTER BUSINESS MAKES THE GREATER GOOD* 179–83 (Oxford Univ. Press 2018) (arguing that systemic challenges like climate change and inequality require corporations to broaden their purpose beyond shareholder primacy); Oliver Hart & Luigi Zingales, *Companies Should Maximize Shareholder Welfare Not Market Value*, 2 J.L. FIN. & ACCT. 247, 249–54 (2017), https://doi.org/10.1561/108.00000022 (proposing governance frameworks that allow management to consider stakeholder welfare, even when it may not increase market value).

[99] *See* Virginia E. Harper Ho, *"Enlightened Shareholder Value": Corporate Governance Beyond the Shareholder-Stakeholder Divide*, 36 J. CORP. L. 59 (2010), https://ssrn.com/abstract=1476116.

[100] *See* George Serafeim, *The Role of the Corporation in Society: Implications for Investors*, HARV. BUS. SCH. WORKING PAPER NO. 14-110 (2014), https://www.hbs.edu/ris/Publication%20Files/14-110_e7a7f1b3-be0d-4992-93cc-7a4834daebf1.pdf (last visited Aug. 11, 2025) (arguing that investors increasingly reward companies that integrate environmental and social considerations into strategy).

[101] *See, e.g.,* REBECCA HENDERSON, *REIMAGINING CAPITALISM IN A WORLD ON FIRE* 54–60 (2020) (discussing the shift toward corporate models that account for societal and environmental impacts).

[102] *See* Lund, *supra* note 5.

[103] *Id.*

debate on the purpose of businesses, specifically whether they should be more shareholder-centered or more broadly shaped.[104]

The most recent chapter in this evolution reflects a challenge to shareholder primacy arising from growing societal, environmental, and governance concerns. In 2019, the Business Roundtable issued a revised statement rejecting the exclusive focus on shareholder wealth and embracing a commitment to stakeholders, including employees, customers, and communities.[105] This is considered a significant shift in corporate governance discourse, reflecting growing concerns that long-term corporate success requires balancing the interests of multiple constituencies rather than prioritizing short-term shareholder gains.[106]

This redefinition of corporate purpose has unfolded alongside significant structural changes in capital markets, particularly in the concentration of share ownership among large institutional investors whose stewardship practices increasingly shape corporate governance priorities. Asset managers such as BlackRock, Vanguard, and State Street wield considerable influence over corporate decisions[107] and are expected to address systemic risks, such as climate change and economic inequality, that affect their entire portfolios and cannot be diversified away.[108] At the same time, this concentration of power raises concerns that institutional investors and fund managers may impose their own values on companies, potentially politicizing corporate governance and overriding the preferences of other shareholders.[109] These dynamics have fueled

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[104] *Id.*

[105] *See* BUSINESS ROUNDTABLE, *Business Roundtable Redefines the Purpose of a Corporation to Promote 'An Economy That Serves All Americans'* (Aug. 19, 2019), https://www.businessroundtable.org/business-roundtable-redefines-the-purpose-of-a-corporation-to-promote-an-economy-that-serves-all-americans (last visited Mar. 15, 2025).

[106] *Id.*

[107] *See* Lucian A. Bebchuk & Scott Hirst, *The Specter of the Giant Three*, 99 B.U. L. REV. 721, 725–26 (2019), https://scholarship.law.bu.edu/faculty_scholarship/641.

[108] *See, e.g.,* Stavros Gadinis & Amelia Miazad, *Corporate Law and Social Risk*, 73 VAND. L. REV. 1401, 1403 (2020), https://cdn.vanderbilt.edu/vu-wordpress-0/wp-content/uploads/sites/278/2020/10/19115823/Corporate-Law-and-Social-Risk.pdf (exploring how institutional investors, particularly asset managers with diversified portfolios, are uniquely vulnerable to systemic risks such as climate change and arguing that these investors are motivated to promote sustainability initiatives to mitigate risks that are difficult to diversify away).

[109] *See* Fisch, Hamdani &s Solomon, *supra* note 92 (analyzing how the rise of passive investing empowers index funds to exert significant influence over corporate governance, potentially leading to a homogenization of corporate policies that may not align with all shareholders' preferences).

debate about the role of passive investing and whether index funds should exercise such significant influence over corporate decision-making.[110]

But just as the ESG movement and the debate on corporate purpose reached their peak, they quickly came under intense scrutiny, particularly in the United States. ESG became increasingly politicized, transforming from a corporate strategy framework into a flashpoint in broader cultural and political battles.[111] Anti-ESG laws proliferated across several Republican-led states,[112] DEI policies faced reevaluation,[113] and companies began retreating from their climate and social commitments.[114] Even former champions of corporate social responsibility, such as BlackRock, the world's largest asset manager, exited certain climate alliances[115] and deliberately distanced themselves from the ESG label.[116]

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[110] For more discussion on passive investing, *See, e.g.,* Ian Appel, Todd A. Gormley & Donald B. Keim, *Passive Investors, Not Passive Owners*, 121 J. FIN. ECON. 111 (2016), https://doi.org/10.1016/j.jfineco.2016.03.003 (finding that passive mutual funds significantly influence corporate governance through voting and engagement, despite limited exit options); K.J. Martijn Cremers & Quinn Curtis, *Do Mutual Fund Investors Get What They Pay For? The Legal Consequences of Closet Index Funds*, 11 VA. L. & BUS. REV. 31 (2016), https://ssrn.com/abstract=2695133 (analyzing the problem of "closet indexing" in mutual funds and its implications for investor protection, governance engagement, and the distinction between active and passive management).

[111] *See, e.g.,* Christopher Hilson, *Climate Change and the Politicization of ESG in the U.S.*, 2024 *FRONTIERS IN POLITICAL SCIENCE,* ecgi.global+4frontiersin.org+4law-economic-studies.law.columbia.edu+4 (analyzing how Republican critics frame ESG as a political imposition and the resulting polarization over ESG norms).

[112] *See* MORRISON & FOERSTER LLP, *Anti-ESG Legislation*, https://www.mofo.com/esg-resources/anti-esg-legislation (last visited Feb. 10, 2025); Karin Rives, *Dozens of New State Anti-ESG Bills Introduced; Federal Legislation Expected*, S&P GLOBAL (Jan. 31, 2025) https://www.spglobal.com/market-intelligence/en/news-insights/articles/2025/1/dozens-of-new-state-antiesg-bills-introduced-federal-legislation-expected-87342102 (last visited Feb. 10, 2025).

[113] *See, e.g.,* ASSOC'D PRESS, *These U.S. Companies Are Pulling Back on Diversity Initiatives*, TIME (Jan. 24, 2025), https://time.com/7209960/companies-rolling-back-dei/ (last visited Feb. 10, 2025).

[114] *See* Kenneth P. Pucker, *Companies Are Scaling Back Sustainability Pledges. Here's What They Should Do Instead*, HARV. BUS. REV. (Aug. 2024), https://hbr.org/2024/08/companies-are-scaling-back-sustainability-pledges-heres-what-they-should-do-instead.

[115] *See, e.g.,* Silla Brush, Saijel Kishan & Alastair Marsh, *BlackRock Exits Major Climate Group Amid Wall Street Exodus*, BLOOMBERG LAW (Jan. 10, 2025), https://news.bloomberglaw.com/ip-law/blackrock-exits-major-climate-group-amid-wall-street-exodus (last visited Feb. 6, 2025); Jack Pitcher, *BlackRock's 'Woke' Era Is Over: Asset Manager Has Exited Climate Groups and Eliminated Diversity Targets as It Tries to End ESG Controversy*, WALL ST. J. (Mar. 2, 2025, 5:30 AM ET), https://www.wsj.com (last visited Mar. 3, 2025).

[116] *See* Isla Binnie, *BlackRock's Fink Says He's Stopped Using 'Weaponised' Term ESG*, REUTERS (June 26, 2023), https://www.reuters.com/business/sustainable-business/blackrocks-fink-says-hes-stopped-using-weaponised-term-esg-2023-06-26/ (last visited Mar. 3, 2025).

This article argues, however, that despite this backlash, sustainability and the ESG movement have already left a lasting imprint on corporate governance. Recent developments suggest that traditional governance structures, while still dominant, are no longer sufficient to address the multi-dimensional risks and responsibilities corporations face today. What is emerging, therefore, is a broader governance paradigm: one that this paper will refer to as *corporate sustainability governance* and will explore next. This evolving model is shaped by both regulatory mandates and voluntary corporate initiatives, and it can be applied not only to climate-related issues but also to a wide range of social concerns, including human rights, labor standards, and supply chain due diligence.

3. Regulatory Drivers of Corporate Sustainability Governance

Building on the preceding discussion of the emergence of corporate sustainability governance, this chapter examines one side of the forces driving this shift: the influence of emerging global regulatory regimes. From climate disclosure mandates to social due diligence requirements, these frameworks have already altered corporate governance, often in ways that have gone unnoticed. They form a central pillar of corporate sustainability governance, a model in which environmental and social considerations are integrated into board oversight, strategic planning, and accountability mechanisms.

Although the majority of the 20th century saw corporate governance and law focused on shareholder returns, recent years have seen a call to incorporate sustainability and stakeholder interests into this model. Early efforts to "regulate" sustainability were voluntary (e.g. Global Reporting Initiative standards in the 2000s), but now there is a growing number of mandatory frameworks that compel companies, including U.S. multinationals, to disclose and manage their sustainability impacts. These developments mark a shift in the legal treatment of sustainability: no longer marginal or altruistic, sustainability is increasingly regarded as a core part of corporate governance and fiduciary responsibility.

This section discusses significant regulatory models, such as those developed by the European Union, the United States, and global standard-setters, and outlines how they incorporate

sustainability into board duties, risk oversight, compliance mechanisms, and disclosure frameworks. While some authors have framed these developments as evidence of an emerging climate governance model,[117] this paper argues that the changes extend further, encompassing a broader range of social and environmental issues. The term corporate sustainability governance aims to capture the full scope of this transformation. Even as the term "ESG" faces reputational fatigue, the legal and institutional infrastructure supporting sustainability governance is already in place. The regulations discussed below reflect not a passing trend, but a lasting transformation in some systems of how companies are governed.

3.1. From Transparency to Norms: The Role of Regulations in Shaping Governance

Typically, disclosure regulations are descriptive, as they require companies to release certain information about their activities, financial situation, and risk factors, rather than commanding particular actions.[118] They compel transparency, mainly to allow investors to make informed decisions, instead of compelling companies to act in a particular manner. However, these same regulations can end up producing normative effects over time. For example, the U.S. Securities and Exchange Commission's (SEC) Regulation S-K requires public companies to disclose material information about, among other things, executive compensation. It does not say how much a company should pay its executives, but the resulting transparency from this mandate may lead firms to adjust their compensation structures after investors' scrutiny or peer comparisons.[119]

[117] *See* Harper Ho, *supra* note 10.

[118] *See* Allen Ferrell, *Mandatory Disclosure and Stock Returns: Evidence from the Over-the-Counter Market*, 36 J. LEGAL STUD. 213 (2007), https://doi.org/10.1086/511898 (explaining that disclosure rules are generally intended to inform investors rather than compel specific corporate conduct); Cass R. Sunstein, *Informational Regulation and Informational Standing: Akins and Beyond*, 147 U. PA. L. REV. 613 (1999), https://scholarship.law.upenn.edu/penn_law_review/vol147/iss3/2 (arguing that informational mandates can, over time, produce behavioral changes by shaping norms and market expectations).

[119] *See* 17 C.F.R. § 229.402 (2025) (Regulation S-K, Item 402) (requiring detailed disclosure of executive compensation, including total compensation and its components, for certain executives).

The same analysis can be applied to emerging sustainability regulations. The ones born in the United States, such as the SEC climate disclosure rules and the California climate disclosure laws, tend to be more descriptive, despite lawsuits challenging their potential prescriptive reach.[120] Some other regimes, mainly from the European Union, have taken on a hybrid character, embedding some accountability obligations within disclosure rules.[121] These instruments go beyond transparency and make companies set up specific processes and structures across their operations and supply chains. However, this section shows that regardless of being descriptive or prescriptive, these new regulatory frameworks are already reshaping corporate governance by elevating sustainability issues to matters of board-level oversight, risk management, and strategic decision-making. Several key instruments are examined to exemplify this trend.

3.1.1. EU's Corporate Sustainability Reporting Directive (CSRD)

The European Union has emerged as a global leader in developing a regulatory framework for sustainability, anchored in its Green Deal, a comprehensive plan to achieve a sustainable and climate-neutral economy by 2050.[122] One of the most important legislative components of this effort is the Corporate Sustainability Reporting Directive (CSRD), adopted in November 2022.[123] It is a landmark regulation dramatically expanding mandatory environmental and social disclosures.[124] It replaces the 2014 Non-Financial Reporting Directive with the goal of raising

[120] *See U.S. Chamber of Com. v. SEC*, No. 24-60152 (5th Cir. filed Mar. 8, 2024) (challenging the SEC's climate disclosure rules as exceeding the agency's statutory authority and compelling speech in violation of the First Amendment); *Cal. Chamber of Com. v. Cal. Air Res. Bd.*, No. 2:23-cv-02312 (E.D. Cal. filed Oct. 7, 2023) (challenging California's S.B. 253 and S.B. 261 as unconstitutional compelled speech and extraterritorial regulation).

[121] *See* Laura Iozzelli & María del Carmen Sandoval Velasco, *Mandatory or Voluntary? The Hybrid Nature of Sustainability Disclosure in the EU's Corporate Sustainability Reporting Directive (CSRD)*, FLORENCE SCH. BANKING & FIN., EUR. UNIV. INST. (Sept. 28, 2023), https://fbf.eui.eu/publication/mandatory-or-voluntary-the-hybrid-nature-of-sustainability-disclosure-in-the-eus-corporate-sustainability-reporting-directive-csrd/.

[122] *See* COUNCIL OF THE EUROPEAN UNION, *European Green Deal*, https://www.consilium.europa.eu/en/policies/european-green-deal/ (last visited Mar. 31, 2025).

[123] *See* Directive (EU) 2022/2464 of the European Parliament and of the Council of 14 Dec. 2022, Amending Regulation 537/2014, Directive 2004/109/EC, Directive 2006/43/EC & Directive 2013/34/EU, as Regards Corporate Sustainability Reporting, 2022 O.J. (L 322) 15, https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A32022L2464 (last visited Mar. 7, 2025).

[124] *See* EUROPEAN PARLIAMENT, *Review of the Non-Financial Reporting Directive*, *Legislative Train* (Apr. 21, 2021) ("[T]he Corporate Sustainability Reporting Directive (CSRD)… aims to revise and strengthen the existing rules introduced by the Non-Financial Reporting Directive (NFRD), and to bring—over time—sustainability reporting

sustainability reporting to the same level as financial reporting.[125] Initially expected to apply to approximately 50,000 companies in the EU and, notably, around 3,000 non-EU companies with substantial operations in the European market,[126] the CSRD introduces detailed sustainability reporting obligations through the European Sustainability Reporting Standards (ESRS).[127]

However, in February 2025, the EU proposed amendments to the CSRD focused mainly on two points: removing small and medium companies from the directive's scope, by focusing on firms with more than 1,000 employees,[128] and giving more time for compliance. The idea was to ease administrative burdens and improve the competitiveness of European businesses.[129] Although the final form of the amendments is still under negotiation, the core structure of the CSRD remains intact, especially for large companies and non-EU firms operating in the EU market.[130] As such, thousands of U.S.-based multinationals are still expected to fall under the directive's requirements over the next several years.[131]

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on a par with financial reporting."), available at https://www.europarl.europa.eu/legislative-train/theme-a-european-green-deal/file-review-of-the-non-financial-reporting-directive (last visited Aug. 11, 2025).

[125] *Id.*

[126] SUSTAINABLE BRANDS, *CSRD to Affect 3,000 U.S. Companies with Significant EU Operations* (2023), https://sustainablebrands.com/read/finance-investment/how-the-eu-s-csrd-will-affect-3-000-us-companies (last visited Mar. 7, 2025).

[127] *See* UNITED NATIONS ENVIRONMENT PROGRAMME FINANCE INITIATIVE, *European Sustainability Reporting Standards (ESRS): Interoperability Package Supports CSRD/ESRS Implementation*, https://www.unepfi.org/impact/interoperability/european-sustainability-reporting-standards-esrs/ (last visited Aug. 11, 2025).

[128] *See* EUROPEAN COMM'N, *Proposal for a Directive of the European Parliament and of the Council Amending Directive 2013/34/EU as Regards the Time Limits for the Adoption of Sustainability Reporting Standards for Certain Sectors and for Certain Third-Country Undertakings*, COM (2024) 805 final (Feb. 5, 2025), https://finance.ec.europa.eu/system/files/2024-02/csrd-amendment-proposal-2025_en.pdf. *See also* SKADDEN, ARPS, SLATE, MEAGHER & FLOM LLP, *European Commission Publishes ESG Reporting Omnibus Package* (Feb. 2025), https://www.skadden.com/insights/publications/2025/02/european-commission-publishes-esg-reporting-omnibus-package (last visited Mar. 7, 2025).

[129] *See, e.g.,* Kate Abnett & Julia Payne, *Europe Plans to Ease Sustainability Reporting Rules to Compete Globally*, REUTERS (Feb. 26, 2025), https://www.reuters.com/world/europe/eu-set-propose-sweeping-red-tape-cuts-boost-business-competitiveness-2025-02-26/.

[130] *Id.* (explaining that the proposal aims to alleviate burdens for SMEs while maintaining the overall objectives of the CSRD and continuing to apply to large entities and those with significant EU operations).

[131] *See* Simon Jessop, Kate Abnett and Virginia Furness, *EU Green Finance Rowback Sets Climate Investment Challenge*, REUTERS (Feb. 27, 2025), https://www.reuters.com/world/europe/eu-green-finance-row-back-sets-climate-investment-challenge-2025-02-27/ (last visited Mar. 31, 2025).

For corporations under its scope, the CSRD mandates extensive reporting on environmental, social, and governance matters, with compliance phased in through 2026 under the current rules—or through 2028 under the proposed amendments.[132] A key characteristic of the CSRD is the use of the "double materiality" concept, which requires companies to report not only how sustainability issues affect their financial performance but also how their activities impact society and the environment.[133] This dual lens, different from the single materiality of other regulatory regimes,[134] aims to significantly enhance corporate accountability.

The environmental component of the CSRD, as detailed in the ESRS, requires companies to disclose greenhouse gas (GHG) emissions across Scopes 1, 2, and 3, encompassing comprehensive data from their entire value chain. Firms must also explain how they manage climate risk, including how they adjust to the reality of climate change, fix decarbonization targets, and comply with the goals of the Paris Agreement.[135] Beyond climate, companies need to disclose the actions they have taken to preserve biodiversity, particularly if their operations cause deforestation or ecosystem degradation.[136] They must also report on how they deal with pollution risks, disposal of toxic waste, and water management to prevent environmental harm.[137]

Under the social requirements of the CSRD, also detailed in the ESRS, companies must report on social and governance issues, including workforce treatment, value chain labor practices, and anti-corruption measures.[138] More specifically, firms must disclose data on employee diversity,

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[132] *See* Abnett & Payne, *supra* note 129.

[133] *See* DELOITTE & TOUCHE LLP, *Unpacking the Double Materiality Assessment Under the E.U. Corporate Sustainability Reporting Directive*, Heads Up, Vol. 31, No. 12 (June 27, 2024), https://dart.deloitte.com/USDART/home/publications/deloitte/heads-up/2024/csrd-esrs-double-materiality-assessment (last visited Aug. 11, 2025).

[134] *Id.*

[135] *See* PERSEFONI, *CSRD: A Guide to the Corporate Sustainability Reporting Directive* (Apr. 15, 2024), https://www.persefoni.com/blog/what-is-csrd (last visited May 15, 2025).

[136] *See* Mindy Hauman & Steph Lartey, *Mind the Gap: A Comparative Analysis of the CSRD, the CSDDD and the SFDR as Green Deal 2.0* (2024 to 2029) *Unfolds*, WHITE & CASE LLP (July 8, 2024), https://www.whitecase.com/insight-alert/mind-gap-comparative-analysis-csrd-csddd-and-sfdr-green-deal-20-2024-2029-unfolds (last visited May 10, 2025).

[137] *Id.*

[138] *See* KEY ESG, *An Introductory Guide to the Corporate Sustainability Reporting Directive (CSRD)* (last updated June 2025), https://www.keyesg.com/article/an-introductory-guide-to-the-corporate-sustainability-reporting-directive-csrd/ (last visited Aug. 2, 2025).

pay equity, health and safety measures, and training programs, including gender pay gap and strategies for promoting inclusive workplaces.[139] Under ESRS S2, companies are required to report on significant actual and potential negative impacts on workers in their value chain, including human rights risks such as forced labor or child labor, and on the actions and policies they have in place to address these risks.[140] Firms must also disclose how they engage with local communities and other stakeholders.[141] On anti-corruption and governance, ESRS G1 mandates transparency on whistleblower protections, corporate ethics policies, political lobbying efforts, and anti-bribery programs.[142] Organizations are required to report in detail on risk management systems that avoid fraud, conflicts of interest, or other forms of unethical business practices.

Importantly, the CSRD integrates governance into sustainability reporting. Companies' annual reports must include a sustainability statement approved by their administrative, management, or supervisory bodies, and these bodies are responsible for ensuring that sustainability information is prepared in accordance with CSRD requirements.[143] For U.S. multinationals within CSRD's scope, this means boards will need to formally sign off on sustainability disclosures and oversee sustainability-related risks and performance[144]. The CSRD also requires independent assurance of sustainability information, starting with limited assurance

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[139] *Id.*

[140] *See* EUROPEAN FIN. REPORTING ADVISORY GRP. (EFRAG), *Draft ESRS Set 1 – Social and Governance Standards* (Nov. 2022), https://www.efrag.org/ (last visited Aug. 2, 2025) (summarizing ESRS S1–S4 requirements on workforce, value chain workers, affected communities, and consumers, and ESRS G1 on business conduct).

[141] *Id.*

[142] *See* FINALYSE, *Navigating the Corporate Sustainability Reporting Directive (CSRD) Landscape* (Apr. 8, 2024), https://www.finalyse.com/blog/navigating-the-corporate-sustainability-reporting-directive-csrd/ (last visited Aug. 11, 2025) (explaining that CSRD-aligned ESRS require disclosures on human rights, value chain impacts, and governance policies such as whistleblower protections and anti-bribery programs).

[143] *See* EUROPEAN FIN. REPORTING ADVISORY GRP. (EFRAG), *ESRS 2 – General Disclosures* (Delegated Act annex) (2023), https://www.efrag.org/sites/default/files/media/document/2024-08/ESRS%202%20Delegated-act-2023-5303-annex-1_en.pdf (last visited Aug. 12, 2025) (GOV-5 requiring disclosure of risk management and internal controls over sustainability reporting and how the sustainability statement is prepared)

[144] *See* GLOBAL REPORTING INITIATIVE, *CSRD: Implications for Companies Outside the EU* (2023), https://www.globalreporting.org/media/3fxpjvfp/gri-reporting-outside-eu-final.pdf (last visited Aug. 5, 2025); Michelle Williams, Steve Nickelsburg and Nicolas Friedlich, *US Companies Face Pressure Around Global ESG Disclosure Mandates*, BLOOMBERG LAW (Jan. 14, 2025), https://news.bloomberglaw.com/us-law-week/us-companies-face-pressure-around-global-esg-disclosure-mandates (last visited Aug. 12, 2025) (reporting on CSRD's impact on U.S. multinationals, including governance and assurance implications).

and progressing toward reasonable assurance, complementing the statutory financial audit.[145] This elevates sustainability reporting to a level of scrutiny that necessitates strong governance and risk management systems.

Board oversight is explicitly detailed. For instance, ESRS 2 mandates disclosure of "the governance body or bodies (e.g., the administrative, management, and supervisory bodies) responsible for sustainability matters," including their "expertise and skills," and the board's "involvement in sustainability-related decisions and oversight of material impacts, risks and opportunities."[146] As a result, companies are training directors on ESG issues and, in some cases, appointing board members with specialized sustainability expertise to meet these expectations.[147] Therefore, CSRD's measures push sustainability governance to the top: companies can no longer treat sustainability reporting as an optional or a PR-driven exercise, but rather as a rigorous, board-supervised process integrated with corporate strategy and risk management. Collectively, the CSRD's reporting obligations aim to increase corporate accountability and investors' confidence in companies' social and governance practices.[148]

For example, a U.S.-based manufacturer with significant EU operations may have to disclose its gas emissions, climate transition plan aligned with the Paris Agreement,[149] workforce diversity and pay equity metrics, and the governance structure overseeing these topics. As the

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[145] *See* Mark Segal, *IAASB Releases New International Sustainability Reporting Assurance Standard*, *ESG TODAY* (Nov. 13, 2024), https://www.esgtoday.com/iaasb-publishes-international-sustainability-reporting-assurance-standard/ (last visited Aug. 12, 2025).

[146] *See* EUROPEAN FIN. REPORTING ADVISORY GRP. (EFRAG), *ESRS 2: General Disclosures – Governance Requirements* (2023), https://www.efrag.org/Assets/Download?assetUrl=/sites/webpublishing/SiteAssets/ESRS%202%20Delegated-act-2023-5303-annex-1_en.pdf (last visited Aug. 12, 2025) (summarizing required disclosures on governance bodies responsible for sustainability, their expertise and skills, and board involvement in sustainability-related decisions);

[147] *See* KPMG, *CSRD: What Boards Need to Know* (Apr. 2024), https://kpmg.com/xx/en/home/insights/2024/04/csrd-what-boards-need-to-know.html (last visited Aug. 2, 2025) (noting that companies are training directors on ESG topics and appointing members with sustainability expertise to meet CSRD/ESRS governance expectations).

[148] *See* Andy Bounds, *Companies Count the Cost of Compliance With Green Rules*, FIN. TIMES (May 15, 2024), https://www.ft.com/content/276028dc-a492-44ec-9eee-58d9fb51c159 (last visited Aug. 12, 2025) (reporting that CSRD implementation is prompting governance changes, including enhanced board oversight and director training on ESG).

[149] *See Paris Agreement*, Dec. 12, 2015, T.I.A.S. No. 16-1104, https://unfccc.int/sites/default/files/english_paris_agreement.pdf (last visited Mar. 7, 2025).

requirements represent a great shift from traditional rules, many large U.S. firms have already been preparing for compliance by creating cross-functional teams (legal, finance, procurement, risk, etc.) to collect ESG data and implement new controls.[150]

3.1.2. EU's Corporate Sustainability Due Diligence Directive (CSDDD)

Another important legislative piece in the UE's sustainability regulatory efforts is the Corporate Sustainability Due Diligence Directive (CSDDD), or CS3D, adopted in May 2024.[151] Unlike the CSRD, which focuses on transparency through mandatory disclosure, the CSDDD imposes substantive behavioral obligations: companies must not only report on sustainability risks, but actively work to identify, prevent, and mitigate them.[152] In this way, the CSDDD elevates sustainability governance from a reporting exercise to a legal duty of care to be incorporated in corporate strategy and supply chain management.

Overall, the directive converts some of the long-standing soft law norms, such as elements of the UN Guiding Principles on Business and Human Rights[153] and the OECD Guidelines for Multinational Enterprises,[154] into binding legal requirements.[155] It applies to both large EU

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[150] *See, e.g.,* Heather Horn & Scott Flynn, *Mandatory Sustainability Metrics Reporting Has Arrived in America via Europe*, CPA J. (Dec. 16, 2024), https://www.cpajournal.com/2024/12/16/mandatory-sustainability-metrics-reporting-has-arrived-in-america-via-europe/ (last visited Mar. 31, 2025).

[151] *See* Council of the European Union, *Corporate Sustainability Due Diligence: Council Gives Its Final Approval*, CONSILIUM.EUROPA.EU (May 24, 2024), https://www.consilium.europa.eu/en/press/press-releases/2024/05/24/corporate-sustainability-due-diligence-council-gives-its-final-approval/ (last visited Aug. 12, 2025) (noting that the directive formally entered into force on July 25, 2024, upon its publication in the Official Journal of the European Union).

[152] *See, e.g.,* SKADDEN, *Corporate Sustainability Due Diligence Directive* (July 25, 2024), https://www.skadden.com/insights/publications/2024/07/corporate-sustainability-due-diligence-directive (last visited Mar. 7, 2025).

[153] *See* United Nations Guiding Principles on Business and Human Rights**,** U.N. DOC. HR/PUB/11/04 (2011), https://www.ohchr.org/documents/publications/guidingprinciplesbusinesshr_en.pdf (last visited Aug. 12, 2025)

[154] *See* ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT, *OECD Guidelines for Multinational Enterprises* (2011), https://www.oecd.org/corporate/mne/48004323.pdf (last visited Aug. 12, 2025).

[155] *See* Karin Buhmann, *Shifting Boundaries: A Transnational Legal Perspective on the EU Corporate Sustainability Due Diligence Directive*, TRANSNAT'L LEGAL THEORY (2024), https://research.cbs.dk/files/110596158/Shifting_boundaries_a_transnational_legal_perspective_on_the_EU_Corporate_Sustainability_Due_Diligence_Directive.pdf (last visited Aug. 12, 2025) (arguing that by drawing on the UNGPs and OECD Guidelines, the CSDDD "turns international soft law into hard law").

companies and non-EU companies with significant EU market presence.[156] Specifically, non-EU companies that generate at least €450 million in annual EU turnover are in scope.[157] Additionally, indirect inclusion applies to companies that do not meet the threshold themselves but are the ultimate parent of in-scope EU subsidiaries or control in-scope firms. As a result, thousands of international companies, including many U.S. multinationals, will be required to implement comprehensive sustainability due diligence programs extending across their global operations.[158]

In February 2025, the EU also proposed amendments to the CSDDD. In contrast to the CSRD, for which the amendment proposed to exclude small and medium-sized companies from the scope, the changes to the CSDDD do not alter the company size thresholds. Instead, the amendment reduces the depth of the obligations and extends the time for compliance.[159] More specifically, the proposal limited mandatory supply chain due diligence to Tier 1 suppliers, rather than the entire upstream and downstream value chain, and increases the compliance timeline by an additional year to give companies and Member States more time to prepare.[160] These changes were intended to improve the implementation feasibility and address competitive concerns raised by industry actors and certain States, without compromising the overall objective of the directive to secure corporate responsibility for human rights and environmental impacts.[161] The amendments are not yet final because they are still subject to approval by the European Parliament.[162]

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[156] *See* Am. Bar Ass'n, *The EU Due Diligence Directive: Implications for U.S. Companies*, BUS. L. TODAY (July 15, 2024).

[157] *Id.*

[158] *See* EUROPEAN COMMISSION, *Corporate Sustainability Due Diligence*, https://commission.europa.eu/business-economy-euro/doing-business-eu/sustainability-due-diligence-responsible-business/corporate-sustainability-due-diligence_en (last visited Aug. 2, 2025).

[159] *See* ISS CORP.., *Simplification or Deregulation? Unpacking the Proposed Omnibus Amendment to EU Sustainability Frameworks* (Feb. 26, 2025), https://www.iss-corporate.com/library/simplification-or-deregulation-unpacking-the-proposed-omnibus-amendment-to-eu-sustainability-frameworks/ (last visited July 6, 2025

[160] *Id.*

[161] *See, e.g.,* Jennifer Rankin, *EU Launches 'Simplification' Agenda in Effort to Keep up with US and China*, GUARDIAN (Jan. 29, 2025), https://www.theguardian.com/world/2025/jan/29/eu-launches-simplification-agenda-in-effort-to-keep-up-with-us-and-china (last visited Aug. 2, 2025) (describing Ursula von der Leyen's announcement of an "unprecedented simplification effort" that includes streamlining sustainable reporting and due diligence rules under the EU's Competitiveness Compass initiative).

[162] *Id.*

For companies under its scope, the CSDDD mandates them to identify, prevent, and mitigate actual or potential adverse impacts on human rights and the environment in their own business activities, in their subsidiaries, and in their supply chain.[163] The supply chain encompasses all the tiers (including indirect suppliers) in the current rules and just tier 1 (direct suppliers) if the amendment is approved, significantly narrowing the scope of supply chain responsibility. To effectively comply with this mandate, companies are required to have robust processes to assess risks in their supply chain, take appropriate measures to cease or mitigate harm, and monitor the effectiveness of these actions. For example, a company must ensure that it and its suppliers meet fundamental human rights (no child labor, decent wages, safe working conditions, etc.) and environmental protection standards, even if they exceed the demands of national law in certain nations.[164] Importantly, the directive also introduced a climate change component: large companies will be obliged to adopt a climate transition plan to align their business with the Paris Agreement's 1.5°C target and the EU's climate neutrality goal for 2050.[165] This means boards must consider how the company aims to reduce emissions.

CSDDD includes a special governance dimension for EU-incorporated companies, directing Member States to ensure that directors of in-scope companies have explicit responsibility for overseeing due diligence and integrating sustainability considerations into corporate strategy.[166] This specific governance obligation does not apply to directors of non-EU companies; however, non-EU companies, including American multinationals, must still comply with the due diligence

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[163] *See* Julia Sinnig & Dirk A. Zetzsche, *The EU's Corporate Sustainability Due Diligence Directive: From Disclosure to Mandatory Prevention of Adverse Sustainability Impacts in Supply Chains*, 16 EUR. J. RISK REGUL. 628 (2025), https://doi.org/10.1017/err.2024.100.

[164] *Id.*

[165] *Id.*

[166] *See* Livia Ventura, *Corporate Sustainability Due Diligence Directive: What Are the New Boundaries of the Firm?*, CAMBRIDGE INST. SUSTAIN. LEADERS (Apr. 30, 2024), https://www.cisl.cam.ac.uk/news/blog/corporate-sustainability-due-diligence-directive-what-are-new-boundaries-firm (last visited Aug. 12, 2025) (observing that CSDDD extends director responsibilities to include supply chain impacts and integrates sustainability into core strategy); *Supervisory Mechanisms and Directors' Duties: Innovations in the Proposed EU Directive on Corporate Sustainability Due Diligence*, BUS. & HUM. RTS. RES. CTR. (Aug. 13, 2024), https://www.business-humanrights.org/latest-news/supervisory-mechanisms-and-directors-duties-innovations-in-the-proposed-eu-directive-on-corporate-sustainability-due-diligence/ (last visited Aug. 12, 2025) (highlighting how the CSDDD embeds directors' duties into company law, requiring governance engagement on sustainability and due diligence).

and reporting requirements and may face corporate-level regulatory sanctions and lawsuits if they fail to do so.

The due diligence duty under CSDDD is not a one-time reporting obligation but an ongoing management practice.[167] This includes interacting with stakeholders, establishing grievance mechanisms, and publishing due diligence statements or reports. When a firm identifies that its business or its suppliers are causing human rights abuse or environmental degradation, it must take action to prevent, remediate or reduce such impact. Enforcement will operate on two levels: public regulatory enforcement and civil liability.[168] Member states need to define supervisory authorities for enforcing compliance, which will inspect firms and apply administrative sanctions. The directive calls for "effective, proportionate and dissuasive" sanctions, which could include substantial fines based on a percentage of a company's turnover. In addition, affected individuals and communities are given the right to seek a remedy. The directive requires member states to implement a regime of civil liability that will permit victims of corporate human rights or environmental violations to sue corporations for damages in EU courts if the corporation had not exercised proper due diligence.[169] This private right of action is a significant innovation: it allows an American corporation to be sued in an EU court by foreign workers or communities alleging that the company failed to prevent harm that directly affected them.[170]

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[167] *See* ARTHUR COX, *New Due Diligence Obligations for Corporates Enter into Force* (July 23, 2024), https://www.arthurcox.com/knowledge/new-due-diligence-obligations-for-corporates-enter-into-force/ (last visited Aug. 12, 2025) (explaining that EU companies will be supervised by national authorities under company-law frameworks, whereas non-EU companies are over*See*n by authorities in the Member State where they have a branch or generate highest EU turnover).

[168] *See* PINSENT MASONS, *Corporate Sustainability Due Diligence: Penalties and Enforcement Under the CS3D* (Dec. 10, 2024), https://www.pinsentmasons.com/out-law/guides/corporate-sustainability-due-diligence-penalties-enforcement-cs3d (last visited Apr. 1, 2025).

[169] *See* Moritz Becker et al., *What to Expect from the EU's CSDDD #2: Civil Liability and Litigation Risks*, FRESHFIELDS BRUCKHAUS DERINGER (May 24, 2024), https://sustainability.freshfields.com/post/102j8in/what-to-expect-from-the-eus-csddd-2-civil-liability-and-litigation-risks (last visited Aug. 12, 2025); BAKER MCKENZIE INSIGHT+, *Penalties and Civil Liability Under the CSDDD*, (Apr. 24, 2024), https://insightplus.bakermckenzie.com/bm/environment-climate-change_1/european-union-penalties-and-civil-liability-under-the-cs3d (last visited Aug. 12, 2025) (outlining the conditions for civil liability and emphasizes joint and several liability regimes).

[170] *See* U.S. CHAMBER OF COM., *Analysis of EU CS3D* (Sept. 6, 2023), https://www.uschamber.com/international/analysis-of-eu-cs3d (last visited Apr. 1, 2025).

Most large U.S. companies that do business in Europe meet the CSDDD's threshold.[171] These companies will need to establish comprehensive due diligence programs that span the globe. Practically, U.S. firms must map their supply chains, assess high-risk suppliers or regions, and implement policies contractually requiring suppliers to uphold human rights and environmental standards.[172] They will probably need to conduct periodic audits or inspections of suppliers, provide training or capacity-building, and, in some cases, terminate relationships with non-compliant partners.[173] For many U.S. companies, this will involve expanding their compliance infrastructure; while compliance departments previously focused on areas like anti-bribery or data privacy, they must now incorporate environmental and human-rights specialists.[174] As supply chain oversight will become much more rigorous, companies may invest in supply chain traceability tools and third-party risk monitoring services.[175]

At a governance level, boards of U.S. companies with EU exposure will need to oversee these obligations.[176] They may receive regular updates on sustainability due diligence programs and progress on climate transition plans.[177] Some will delegate a board committee (or stretch an existing audit or risk committee) to oversee the due diligence. Accountability structures are also impacted. The risk of potential civil liability will require U.S. company legal and risk officers to take sustainability risks as seriously as other business risks.[178] One can anticipate that companies

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[171] *See* Am. Bar Ass'n, *supra* note 156.

[172] *Id.*

[173] *See* Cooley LLP, *Impacts for U.S. Companies of the Proposed EU Omnibus Package* (Feb. 26, 2025), https://www.cooley.com/news/insight/2025/2025-02-26-impacts-for-us-companies-of-the-proposed-eu-omnibus-package (last visited Apr. 1, 2025) (noting that CSDDD requires contractual clauses upstream, supplier termination where necessary, and regular due diligence monitoring of high-risk business partners).

[174] *See* DLA PIPER, EU'S *Proposed Directive on Corporate Sustainability Due Diligence: What U.S. Companies Need to Know* (June 2023), https://www.dlapiper.com/en-us/insights/publications/global-esg-alert/2023/eus-proposed-directive-on-corporate-sustainability-due-diligence-what-us-companies-need-to-know (last visited Apr. 1, 2025).

[175] *Id.*

[176] *See* BDO USA, *EU's CSDDD Impact on U.S. Company Supply Chains*, https://www.bdo.com/insights/sustainability-and-esg/eu-s-csddd-impact-on-u-s-company-supply-chains (last visited Apr. 1, 2025).

[177] *Id.*

[178] *See* Luca Enriques, Matteo Gatti & Roy Shapira, *How the EU Sustainability Due Diligence Directive Could Reshape Corporate America* (EUR. CORP. GOVERNANCE INST., Law Working Paper No. 817/2025; BOCCONI LEGAL STUD. RSCH. PAPER No. 5083571; RUTGERS L. SCH. RSCH. PAPER, forthcoming 2025),

that have remediation mechanisms in place (e.g. hotlines or grievance procedures for employees within their supply chain) will resolve issues early and not face lawsuits or enforcement actions. In brief, the CSDDD pressures U.S. companies in Europe to be preventive and accountability-driven when it comes to sustainability.[179] It shifts the focus from merely reporting on ESG issues to actively resolving and improving conditions in supply chains.[180] This will probably create a ripple effect on how U.S. companies manage suppliers worldwide, as many tend to apply the EU standards everywhere for consistency, thereby raising the bar for corporate conduct even in regions without similar laws.[181]

3.1.3. International Sustainability Standards Board (ISSB)

The International Sustainability Standards Board (ISSB), launched in 2021 by the IFRS Foundation, is considered a major step towards creating a global benchmark for corporate sustainability reporting.[182] In June 2023, the ISSB released its first two standards: IFRS S1 (General Requirements for Disclosure of Sustainability-related Financial Information)[183] and IFRS S2 (Climate-related Disclosures).[184] These standards aim to provide investors and capital markets with comparable, consistent sustainability information by leveraging the Task Force on Climate-related

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https://ssrn.com/abstract=5083571 (discussing how the Directive places sustainability risks into legal oversight calculus, prompting boards to receive structured updates, reallocating responsibility to compliance departments, and exposing directors to oversight duty liability).

[179] *Id.*

[180] *See* KPMG INTERNATIONAL, *Global Implications of Due Diligence Acts*, https://kpmg.com/us/en/frv/reference-library/2024/global-implications-of-due-diligence-acts.html (last visited Apr. 1, 2025).

[181] *See* Enriques, Gatti & Shapira, *supra* note 178.

[182] *See* IFRS FOUND., *Inaugural Jurisdictional Guide for the Adoption or Other Use of ISSB Standards* (May 2024), https://www.ifrs.org/content/dam/ifrs/supporting-implementation/adoption-guide/inaugural-jurisdictional-guide.pdf.

[183] *See* IFRS FOUND., *IFRS S1: General Requirements for Disclosure of Sustainability-related Financial Information* (June 2023), https://www.ifrs.org/issued-standards/ifrs-sustainability-standards/ifrs-s1-general-requirements-for-disclosure-of-sustainability-related-financial-information/.

[184] *See* IFRS FOUND., *IFRS S2: Climate-related Disclosures* (June 2023), https://www.ifrs.org/issued-standards/ifrs-sustainability-standards/ifrs-s2-climate-related-disclosures/.

Financial Disclosures (TCFD) and the Sustainability Accounting Standards Board (SASB) and aligning with existing financial reporting frameworks under IFRS.[185]

Although ISSB standards are not compulsory unless adopted by individual jurisdictions, they are rapidly becoming de facto regulatory benchmarks. Jurisdictions representing over half the global economy by GDP, such as the UK, Japan, Singapore, Canada, Australia, Brazil, and Nigeria, have already committed to adopting or aligning with ISSB standards through domestic regulation or guidance.[186] In some cases, such as the UK, regulators have brought forward formal mandates that require listed companies to report in line with ISSB.[187] In Brazil, the norms will become mandatory for publicly traded companies from 2026.[188] In others, regulators are encouraging voluntary alignment.[189] This broad adoption indicates that, despite the expected "Brussels Effect", ISSB is indeed on track to become the global standard for sustainability disclosure in financial markets.[190]

While IFRS S1 and S2 focus on disclosure rather than prescribing corporate behavior, they do include governance expectations that impact how companies conceptualize sustainability internally. Both standards require entities to disclose how the board and management oversee sustainability-related risks and opportunities, how those risks are integrated into overall strategy and risk management processes, and how progress is measured and monitored, including the specific metrics and targets used.[191]

On the content, IFRS S2 is exclusively dedicated to climate-related disclosures, and IFRS S1 has a more extensive system of reporting, covering all the sustainability-related risks and

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[185] *Id.*

[186] *See* IFRS FOUND., *Jurisdictions Representing over Half the Global Economy by GDP Take Steps towards ISSB Standards* (May 2024), https://www.ifrs.org/news-and-events/news/2024/05/jurisdictions-representing-over-half-the-global-economy-by-gdp-take-steps-towards-issb-standards/.

[187] *See* UK Dep't for Energy Sec. & Net Zero, *UK Sustainability Reporting Standards* (SRS), GOV.UK, https://www.gov.uk/guidance/uk-sustainability-reporting-standards (last visited Apr. 6, 2025).

[188] *See* Jennifer Laidlaw, *In This List, December 2024 – Where Does the World Stand on ISSB Adoption?*, S&P GLOB. (Jan. 31, 2025), https://www.spglobal.com/esg/insights/december-2024-where-does-the-world-stand-on-issb-adoption (last visited Feb. 2025).

[189] *Id.*

[190] *See* Stavros & Fregoni, *supra* note 19.

[191] *Id.*

opportunities that could reasonably influence investors' decisions.[192] IFRS S1 requires companies to disclose material information on a wide range of ESG issues, including social risk governance, human capital management, supply chain practices, and ethical behavior, all considering financial materiality.[193] More specifically, it mandates that corporations disclose how sustainability issues are integrated into governance structures, strategic planning, and risk management systems. It also mandates disclosure of procedures used to identify, assess, and monitor sustainability-related risks and opportunities along time horizons. In doing so, IFRS S1 places a blanket assumption that boards and senior management must have control over material sustainability issues, not just climate, but also social and governance issues that impact long-term enterprise value.[194] On the environmental side, IFRS S2 actually requires disclosures on climate-related issues, such as physical and transition risks, climate resilience strategies, greenhouse gas emissions (Scopes 1, 2, and 3), and carbon offset use.[195] Such a broader orientation directly influences the emergence of the corporate sustainability governance, where companies are being called upon to address increasingly wider ranges of non-financial risk and stakeholder concerns as a normal part of governance and disclosure practices.

In practice, ISSB compliance requires firms to maintain internal controls, data systems, and governance arrangements that are the same as for financial reporting.[196] Firms must engage

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[192] *See* IFRS FOUND., *Effects Analysis: General Requirements for Disclosure of Sustainability-Related Financial Information and Climate-Related Disclosures* (June 2023), https://www.ifrs.org/content/dam/ifrs/project/general-sustainability-related-disclosures/effects-analysis.pdf (last visited Aug. 12, 2025) (explaining that IFRS S1 establishes a global baseline for *sustainability-related risks and opportunities* across ESG dimensions—including governance, strategy, risk management, and metrics—while IFRS S2 supplements it with targeted requirements on climate-related financial risks such as physical and transition risks, climate resilience, and Scope 1–3 GHG emissions).

[193] *See* EARTH-SCAN, *IFRS S1 vs IFRS S2: What's the difference?* (July 31, 2025), https://www.earth-scan.com/blog/meaning-issb (last visited Aug. 12, 2025) (noting that IFRS S1 covers all sustainability risks and opportunities, while IFRS S2 focuses purely on climate-related disclosures within the same governance–strategy–risk management–metrics framework).

[194] *Id.*

[195] *See* WORLD RES. INST., *Statement: New Standard from the International Sustainability Standards Board (ISSB) Requires Disclosure of Scope 3 Emissions* (June 26, 2023) (press release), https://www.wri.org/news/statement-new-standard-international-sustainability-standards-board-issb-requires-disclosure-scope-3 (last visited Aug. 2, 2025).

[196] *See* IFRS FOUND., *Using ISSB Standards With the Revised Management Commentary Practice Statement* (June 23, 2025), https://www.ifrs.org/news-and-events/news/2025/06/using-issb-standards-with-management-

cross-functional teams, such as operations, risk, finance, and legal, to make sustainability data accurate and decision-useful.[197] At the same time, boards should oversee these processes and align them with long-term business strategy.[198] Therefore, ISSB standards are already changing boardroom practices, even in countries where legal obligations are still modest.

Although the ISSB does not have enforcement powers comparable to the E.U. or U.S. regulators, jurisdictions that adopt the standards do. Besides that, its widespread adoption by several securities regulators and stock exchanges globally means that companies seeking access to global capital markets will be inclined to adopt the standards, voluntarily or as a listing requirement.[199] Moreover, for multinational corporations, aligning with ISSB standards offers a pragmatic way to satisfy diverse reporting requirements across jurisdictions, as the EU and California, for example, are working toward interoperability with the ISSB framework.[200] In the longer run, the ISSB will release more rules to cover other environmental, social, and governance concerns, including labor rights, human capital, and biodiversity, further establishing its relevance to corporate sustainability governance.

In short, the ISSB illustrates how initially "voluntary" global templates can reach meaningful regulatory effects. By integrating governance disclosures into ordinary corporate reporting, the ISSB is pushing forward the institutionalization of sustainability as a core part of financial oversight and board-level accountability, especially in jurisdictions where regulation is still in transition.

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commentary/ (last visited Aug. 12, 2025) (noting that IFRS S1 sustainability disclosures are embedded within general-purpose financial reports and can integrate into the same controls and governance processes).

[197] *Id.*

[198] *See* ENHESA, *Understanding the ISSB Standards* (July 1, 2025), https://www.enhesa.com/resources/article/understanding-the-issb-standards/ (last visited Aug. 2, 2025) (explaining that ISSB standards require disclosures on governance bodies, such as boards or committees, and internal controls managing sustainability risks akin to financial oversight structures).

[199] *See* Huw Jones, *Momentum Building Behind Global Company Climate Disclosures, Standards Body Says*, REUTERS (May 28, 2024), https://www.reuters.com/business/environment/momentum-building-behind-global-company-climate-disclosures-standards-body-says-2024-05-28/ (last visited Aug. 12, 2025).

[200] *See* INSTITUTIONAL S'HOLDER SERVS. (ISS), *A Global Baseline? How to Navigate Interoperability Across Sustainability Reporting Rules* (Mar. 11, 2024), https://www.iss-corporate.com/library/a-global-baseline-how-to-navigate-interoperability-across-sustainability-reporting-rules/ (last visited May 13, 2025).

3.1.4. SEC Climate Disclosure

In the United States, the main regulatory sustainability efforts came from the Securities and Exchange Commission (SEC), which in March 2024 adopted landmark rules requiring public companies to provide detailed climate-related disclosures in their annual reports and registration statements.[201] However, the SEC rules are no longer being implemented. They were promptly challenged in court, and under the new American administration the agency chose to abandon their defense.[202] Despite this outcome, the rules had already influenced corporate behavior, as many companies began preparing to comply during the two years between the proposal and their adoption.[203]

In addition, States laws may fill out the gap left by the federal government. At the state level, California became the first in the nation to enact climate disclosure legislation,[204] which is also being challenged in court.[205] California's pioneering climate disclosure laws, mandating coverage of greenhouse gas emissions and climate-related financial risks, are expected to exert influence beyond its borders through what is commonly referred to as the "California Effect," whereby stricter regulatory standards in a major economic jurisdiction prompt similar legislation

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[201] *See* U.S. SEC. & EXCH. COMM'N, *The Enhancement and Standardization of Climate-Related Disclosures for Investors*, Release No. 33-11042, 87 Fed. Reg. 21334, 21336–38 (proposed Mar. 21, 2022).

[202] *See Republican-Led States File Lawsuit to Block SEC's Climate Disclosure Rule*, UTILITY DIVE (Mar. 8, 2024), https://www.utilitydive.com/news/10-republican-states-challenge-final-sec-climate-disclosure-rule/709871/; Andrew Ramonas, *Nine More States Target SEC Climate Reporting Rules in Court*, BLOOMBERG LAW (Mar. 12, 2024, 12:28 PM), https://news.bloomberglaw.com/esg/nine-more-states-join-republican-lawsuits-over-sec-climate-rules (last visited May 15, 2025).

[203] *See* Raquel Fox, Marc S. Gerber, & Caroline S. Kim, *Preparing Now for the SEC's New Climate Rules*, HARV. L. SCH. F. ON CORP. GOVERNANCE (May 22, 2024), https://corpgov.law.harvard.edu/2024/05/22/preparing-now-for-the-secs-new-climate-rules/ (last visited Aug. 12, 2025).

[204] *See* CERES, California's First-in-the-Nation Climate Disclosure Legislation Sets New Standard for Corporate Transparency (Sept. 11, 2023), https://www.ceres.org/news-center/press-releases/californias-first-nation-climate-disclosure-legislation-sets-new (last visited June 5, 2025).

[205] *See* VINSON & ELKINS LLP, *Ongoing Legal Battle Over California's Climate-Related Disclosure Laws* (Feb. 7, 2025), https://www.velaw.com/insights/ongoing-legal-battle-over-californias-climate-related-disclosure-laws-district-court-dismisses-supremacy-clause-and-extraterritoriality-claims-in-u-s-chamber-of-commerce-v-carb/ (last visited June 5, 2025).

elsewhere.[206] That trend is already visible in other states: New York's Climate Corporate Data Accountability Act (S.3456) proposes mandatory disclosure of Scope 1–3 emissions; New Jersey has introduced S.4117 with analogous goals; and Colorado is considering HB 25-1119, which would require large companies to disclose greenhouse gas emissions starting in 2028.[207] This article will examine the SEC and California regimes in detail, as they remain the most consequential developments in U.S. sustainability disclosure despite ongoing legal challenges.

The SEC's rules required companies to disclose material climate-related risks (physical and transition risks) and their actual or potential impacts on the business, strategy, and financial results.[208] They also needed to disclose any climate-related targets or transition plans and the associated expenditures or impacts on financial estimates.[209] For large accelerated filers (public float of $700 million or more) and accelerated filers (public float of $75 million to less than $700 million), the SEC required reporting of Scope 1 and Scope 2 emissions (direct emissions and energy purchases) if material. There was also a requirement for large accelerated filers to seek an independent assurance report—limited assurance at first, moving to reasonable assurance after a transition period.[210]

Additionally, companies had to include certain climate-related financial metrics in their audited financial statements, such as costs associated with severe weather events or efforts to reach

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[206] *See* Jens Frankenreiter, *Cost-Based California Effects*, in *The California Effect: Regulatory Interdependence in the U.S.* 1098–99 (Yale J. Reg. 2022) (describing how California's environmental regulations spread to other jurisdictions despite no formal obligation); Andrew McDonald, *Cowboy State Policy Goes West*, 22 Policy Renewal 13, 14 (2023) (explaining the California Effect in climate regulation context).

[207] *See* Ropes & Gray, *Climate Disclosure Bills Reintroduced in New York: Fast Facts and Take-Aways* (Feb. 3, 2025), https://www.ropesgray.com/en/insights/viewpoints/102jyry/climate-disclosure-bills-reintroduced-in-new-york-fast-facts-and-take-aways (last visited Aug. 9, 2025) (discussing S.3456 requiring Scope 1–3 emissions reporting); REGULATORY & COMPLIANCE, *State Climate Disclosure Bills—A Growing Trend?* (Apr. 10, 2025), https://www.regulatoryandcompliance.com/2025/04/state-climate-disclosure-bills-a-growing-trend (last visited Aug. 9, 2025) (summarizing New Jersey's S.4117 and Colorado's HB 25-1119 requiring GHG emissions disclosures).

[208] *See* Catherine M. Clarkin, C. Michelle Chen & June M. Hu, *Key Implications of SEC's Climate-Related Disclosure Rules*, HARV. L. SCH. F. ON CORP. GOVERNANCE (Apr. 1, 2024), https://corpgov.law.harvard.edu/2024/04/01/key-implications-of-secs-climate-related-disclosure-rules/ (last visited June 5, 2025).

[209] *Id.*

[210] *See* Chloe Field & Cynthia Hanawalt, *The SEC's Final Climate Disclosure Rule: Key Requirements, and the Materiality Threshold*, CLIMATE L. BLOG (Mar. 11, 2024), https://blogs.law.columbia.edu/climatechange/2024/03/11/the-secs-final-climate-disclosure-rule-key-requirements-and-the-materiality-threshold/.

climate goals.[211] These climate disclosures aim to be "consistent, comparable, and decision-useful" for investors, reflecting investor demand for reliable information on climate risks.

At the governance level, the SEC rules explicitly required companies to show how their board of directors oversees climate-related risks, including committee responsibilities and frequency of discussions.[212] They also required reporting on management's role in assessing and managing such risks, identifying the responsible individuals or teams, and describing how they interact with the board.[213] These provisions encouraged the integration of climate oversight into the broader governance structure. Moreover, by requiring disclosure of the actual or likely material impacts of climate risks on business strategy, financial performance, and long-term planning, the rules made it difficult to silo climate considerations within sustainability departments.[214] So, boards and executives would need to incorporate these issues into strategic decision-making. In addition, if a company adopted a climate-related target or transition plan, it had to disclose how progress would be monitored, the costs of achieving it, and its effects on financial plans, further embedding climate considerations into governance practices.[215]

But it is not just that. Disclosure of climate-related financial impacts and emissions (including audited metrics and assurance for Scope 1 and 2 for some filers) will require new data governance systems, strong internal controls, and oversight by audit committees and legal/compliance teams.[216] This means that boards will need to ensure that companies establish robust internal processes for collecting, verifying, and disclosing climate data, similar to financial

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[211] *Id.*

[212] *See* Deloitte, *Materiality, Interoperability Aspects of Climate Reporting Merit Continued Focus*, DELOITTE-WSJ SUSTAINABLE BUSINESS (May 21, 2024), https://deloitte.wsj.com/sustainable-business/materiality-interoperability-aspects-of-climate-reporting-merit-continued-focus-387446db (last visited Aug. 2, 2025) (noting that the rule requires companies to develop clear governance structures and internal controls for climate reporting, emphasizing board accountability in climate risk oversight).

[213] *Id.*

[214] See Latham & Watkins, *The SEC's Final Climate Disclosure Rule—Board and Management Oversight* (Mar. 21, 2024), available via Westlaw (last visited Aug. 2, 2025) (explaining that the final rule requires disclosure of board oversight of climate-related risks, including the responsible committee and how the board is informed, as well as management's role and expertise in assessing and managing these risks, under Regulation S-K Item 1501(a) and (b)).

[215] *Id.*

[216] *See* Gadinis, *supra* note 97.

reporting systems under the Sarbanes-Oxley.[217] Lastly, there is an expectation for greater directors' liability and possible shareholder scrutiny.[218] While the rules do not impose new fiduciary duties on directors, disclosure failures could lead to SEC enforcement and shareholder derivative suits.[219] Therefore, directors had to ensure adequate oversight of climate disclosures, especially given the litigation risk and great shareholder attention to climate governance.

Outside the climate sphere, the SEC has adopted only limited and largely principles-based requirements on social issues. Since 2020, public companies have been required to provide a general description of their human capital resources, but no standardized metrics apply across all issuers.[220] Although the SEC has discussed enhancing human capital disclosures, such as workforce diversity and turnover,[221] these initiatives are unlikely to advance in the near term.[222] The agency also mandates disclosure in narrow areas, such as conflict minerals[223] and resource extraction payments,[224] which address specific social or governance concerns but stop short of establishing a broad, standardized framework. In practice, many companies publish voluntary ESG reports, yet

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[217] *Id.*

[218] *See* CLEARY GOTTLIEB, *Potential Litigation Risks Associated with the SEC's Proposed Rule on Climate-Related Disclosures* (Sept. 14, 2022), https://www.clearygottlieb.com/news-and-insights/publication-listing/potential-litigation-risks-associated-with-the-secs-proposed-rule-on-climate-related-disclosures (last visited Aug. 2, 2025) (cataloging possible state and federal litigation theories triggered by climate disclosure failures).

[219] *Id. See also* MINTZ, *Caremark Liability Following the SEC's New ESG Reporting Obligations* (Dec. 16, 2022), https://www.mintz.com/insights-center/viewpoints/2301/2022-12-21-caremark-liability-following-secs-new-esg-reporting (last visited Aug. 2, 2025) (identifying the intersection of ESG disclosure reviews with Caremark-type oversight duties).

[220] *See* Regulation S-K, 17 C.F.R. § 229.101(c)(2) (2023) (requiring disclosure of human capital resources, including any measures or objectives that the registrant focuses on in managing the business

[221] *See* U.S. SEC. & EXCH. COMM'N, Inv. Advisory Comm., *Recommendation Regarding Human Capital Management Disclosure* (Sept. 21, 2023), https://www.sec.gov/files/spotlight/iac/20230921-recommendation-regarding-hcm.pdf (last visited Aug. 2, 2025).

[222] *See* Zoya Mirza, SEC's ESG Greenwashing, Human Capital Disclosure Rules Pushed to October, *ESG DIVE* (July 10, 2024), https://www.esgdive.com/news/secs-esg-greenwashing-human-capital-disclosure-rules-pushed-to-october/721012/ (last visited Aug. 2, 2025) (noting that the SEC delayed human capital management disclosure rulemaking from April to October 2024); Soyoung Ho, SEC Plans to Issue 4 Proposals by End of 2024, *Thomson Reuters* (Aug. 7, 2024), https://tax.thomsonreuters.com/news/sec-plans-to-issue-4-proposals-by-end-of-2024/ (last visited Aug. 2, 2025) (highlighting that the upcoming regulatory agenda contains no human capital proposals, meaning any substantive action is unlikely in the near term).

[223] *See* 17 C.F.R. §§ 240.13p-1, 240.13q-1 (2023

[224] *See* U.S. SEC. & EXCH. COMM'N, *Rule for Resource Extraction Issuers* (Dec. 16, 2020), https://www.sec.gov/news/press-release/2020-311 (last visited Aug. 2, 2025).

climate remains the only ESG topic for which the SEC issued comprehensive, prescriptive disclosure rules. This approach has effectively separated climate risk, subject to these detailed rules, from other ESG factors, which remain largely voluntary or guided only by general materiality principles.

3.1.5. California Climate Laws

California's climate disclosure laws are even broader in scope than the SEC's rules, as they apply to large private companies as well as public ones and mandate reporting of Scope 3 greenhouse gas emissions, in addition to Scopes 1 and 2.

California's SB 253 requires large companies "doing business" in California—both public and private—with over $1 billion in annual revenues to publicly report their emissions annually.[225] This includes Scope 1 (direct emissions), Scope 2 (indirect emissions from purchased energy), and Scope 3 (emissions from the value chain) following the Greenhouse Gas Protocol.[226] Originally, the law required Scope 1 and 2 disclosures to begin in 2026 (covering 2025 emissions), with Scope 3 reporting following in 2027. However, amendments enacted through SB 219 grant the California Air Resources Board (CARB) discretion to set the timing of Scope 3 reporting through future regulations, eliminating the original fixed deadline.[227]

The law also introduces a phased independent third-party assurance for emissions reports. Limited assurance is required for Scopes 1 and 2, progressing to reasonable (a more rigorous audit-level check) assurance by 2030. For Scope 3 emissions, limited assurance will be required by 2030. The legislature also made several administrative adjustments with SB 219,[228] including allowing companies to report emissions at the parent-entity level and eliminating upfront filing fees. The

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[225] *See* Cal. S.B. 253, 2023–2024 Reg. Sess. (Cal. 2023), https://leginfo.legislature.ca.gov/faces/billNavClient.xhtml?bill_id=202320240SB253

[226] *Id.*

[227] Senate Bill 219, *Greenhouse Gases: Climate Corporate Accountability: Climate-Related Financial Risk*, ch. 766, § 38532–33, 2023–24 Reg. Sess. (Cal. 2024) (enacted Sept. 27, 2024), summarized in Alice Roberts & Amy Malick, *California Amends Its Climate Corporate Data Accountability Package: SB 219*, *Ramboll Insights* (Oct. 2, 2024), https://www.ramboll.com/en-us/news/california-amends-climate-corporate-data-accountability-package (last visited Aug. 12, 2025).

[228] Cal. S.B. 219, 2023–2024 Leg., Reg. Sess. (2024).

CARB will likely release proposed implementing regulations by the end of 2025 and will oversee the development and enforcement of the reporting framework.[229]

California's SB 261, the Climate-Related Financial Risk Act, complements SB 253 by focusing not on emissions accounting but on climate-related financial risk disclosure.[230] It applies to companies with over $500 million in annual revenue doing business in California (a lower threshold than SB 253).[231] SB 261 requires covered companies to prepare a biennial climate-related financial risk report disclosing the material climate risks they face—both physical risks (such as the impacts of extreme weather events) and transition risks (such as regulatory changes, market shifts, or evolving technologies)—as well as the measures the company is taking to mitigate or adapt to those risks.[232] The reports, which will be publicly available, should align with widely accepted frameworks such as the Task Force on Climate-related Financial Disclosures (TCFD).[233]

The first climate risk reports are due by January 1, 2026, if no change is made, and then every two years thereafter. CARB will contract with a climate reporting organization to review disclosures, publish a biennial summary analyzing systemic and sector-specific risks, and identify inadequate or noncompliant reports.[234] SB 219, adopted in 2024, eliminated the previously required filing fee and clarified that CARB may impose administrative penalties for noncompliance.[235] Notably, SB 261 is about transparency of climate risk management; it does not dictate specific

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[229] *See* SKADDEN, *State of Play: California Amends Climate Disclosure Rules Under SB 219* (Oct. 3, 2024), https://www.skadden.com/insights/publications/2024/10/state-of-play-california-amends-climate-disclosure-rules (last visited June 5, 2025).

[230] Cal. S.B. 261, Climate-Related Financial Risk Act, 2023–2024 Leg., Reg. Sess. (Cal. 2023).

[231] *See* Madison Olson, *Coming Soon: "Doing Business" in California Will Require Companies to Disclose Climate Risk and Emissions Reports*, AM. U. BUS. L. REV. (Oct. 25, 2023), https://aublr.org/2023/10/coming-soon-doing-business-in-california-will-require-companies-to-disclose-climate-risk-and-emissions-reports/ (last visited May 15, 2025).

[232] *See* Linklaters LLP, *California Legislature Passes Landmark Climate Disclosure Laws* (Sept. 20, 2023), https://www.linklaters.com/en-us/knowledge/publications/alerts-newsletters-and-guides/2023/september/20/california-legislature-passes-landmark-climate-disclosure-laws (last visited May 15, 2025).

[233] *See* TCFD, *supra* note 13.

[234] *See* PERSEFONI, *California SB 253 and SB 261: What Businesses Need to Know*, Persefoni Blog (Jan. 24, 2025), https://www.persefoni.com/blog/california-sb253-sb261 (last visited May 15, 2025)..

[235] *See* KATTEN MUCHIN ROSENMAN LLP, *SB 219 Makes Important Updates to California Climate Disclosure Regime* (Sept. 2024), https://katten.com/sb-219-makes-important-updates-to-california-climate-disclosure-regime.

reduction targets or actions, but by exposing risks and strategies, it encourages companies to plan for climate impacts.

California's laws include significant enforcement mechanisms. Firms that fail to comply with the rules may face civil penalties, including fines of up to $500,000 per year under SB 253 for failing to report or misrepresenting emissions data, and up to $50,000 per year under SB 261 for failing to submit or inadequately preparing a climate risk report.[236] Recognizing the challenge of launching disclosures before final rules are in place, CARB has indicated it will exercise enforcement discretion for SB 253's first year: if companies make good-faith efforts to collect emissions data, it will not penalize incomplete first-year reports.[237] In subsequent years, however, full compliance will be expected. Although SB 261's enforcement process remains less defined, penalties may also be imposed by CARB or the California Attorney General. Because the disclosures are public, non-compliance also carries reputational risks, enabling investors, regulators, and advocacy groups to hold companies accountable.[238]

The implications of California's laws for corporate governance and compliance are significant. The laws are compelling companies, including many large private businesses, to strengthen their governance of climate issues. With SB 253, they must implement robust emissions accounting across their entire value chain, as Scope 3 extends into supplier and customer activities.[239] This requires new internal controls, data management systems, and possibly the engagement of specialist consultants or software to measure emissions. Boards of directors and top executives will need to be involved in oversight of these efforts, since annual emissions reports with third-party assurance will publicize the company's carbon footprint.[240] Many companies

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[236] *See* CARBONCHAIN, *California Climate Disclosure Rules: What Companies Need to Know* (2023), https://www.carbonchain.com/carbon-reporting/california-disclosure-sb253-sb261.

[237] *See* SIDLEY AUSTIN LLP, *CARB Releases First Enforcement Notice for the Climate Corporate Data Accountability Act* (Dec. 19, 2024), https://www.sidley.com/en/insights/newsupdates/2024/12/carb-releases-first-enforcement-notice-for-the-climate-corporate-data-accountability-act.

[238] *See* DELOITTE, *California Climate Legislation Update: Reporting Deadlines Extended, New Guidance Coming* (Oct. 2024), https://dart.deloitte.com/USDART/home/publications/deloitte/heads-up/2024/california-climate-legislation-update-reporting-deadline.

[239] *See* Cal. S.B. 253, *supra* note 225.

[240] *Id.*

establish internal sustainability teams or steering committees to ensure compliance with SB 253, often reporting up to the CFO or audit committee (given the assurance/audit component).[241]

SB 261 similarly elevates climate risk to a governance-level concern. Companies need to analyze and publicly report on climate-related risks and mitigation strategies, which typically involve input from many parts of the firm: risk management, finance, operations, and sustainability teams.[242] Boards will likely review and approve these risk reports, as they resemble other statutory disclosures in importance.[243] In practice, California's requirements encourage companies to integrate climate considerations into their corporate strategy and governance.

Compliance structures are also being adapted accordingly: companies are aligning their reporting processes with TCFD principles, enhancing cross-department coordination (e.g. legal, EHS, operations, and finance working together on disclosures), and scheduling regular audits of emissions data.[244] Finally, because California's economy is so large, these laws have extraterritorial influence. Many U.S. companies nationwide (and even foreign companies) that generate significant revenue in California must comply, effectively setting a de facto standard.[245] Therefore, SB 253 and SB 261 are reshaping corporate behavior by making climate disclosure a legal obligation, prompting stronger oversight from boards, more rigorous compliance mechanisms, and greater transparency around climate performance and risk management.

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[241] *See* Henry Engler, *Companies Need to Integrate Climate Reporting Across Functions to Comply with California's New Law*, THOMSON REUTERS (Oct. 19, 2023), https://www.thomsonreuters.com/en-us/posts/esg/california-climate-reporting-law/ (last visited Aug. 2, 2025).

[242] *See* Cal. S.B. 261, *supra* note 230.

[243] *See* Engler, *supra* note 241.

[244] *See* CAL. AIR RES. BD., *California Corporate Greenhouse Gas Reporting and Climate-Related Financial Risk Disclosure Programs: Frequently Asked Questions Related to Regulatory Development and Initial Reports* (July 9, 2025), https://ww2.arb.ca.gov/sites/default/files/2025-07/FAQs%20Regarding%20California%20Climate%20Disclosure%20Requirements.pdf (last visited Aug. 2, 2025) (explaining compliance expectations, including alignment with TCFD and internal coordination across departments).

[245] *See* CAL. ENV'T PROT. AGENCY, *California Climate Policies: Leading the Nation and the World* (2024), https://calepa.ca.gov/climate/california-climate-policies/ (last visited Aug. 2, 2025) (describing the state's global economic influence and how its climate laws shape standards beyond its borders).

3.1.6. Comparing Regulatory Models of Sustainability Governance

Despite different scopes, European regulations, ISSB standards, SEC climate rules and California's laws, all signal a growing regulatory insistence on corporate sustainability accountability. A clear common theme is transparency: each framework forces companies to disclose information on sustainability, whether on carbon emissions, climate risks, or human rights impacts, which was largely voluntary until recently. They respond to demands from investors,[246] consumers,[247] and civil society[248] for consistent and reliable data on sustainability performance.

Another shared emphasis is on board and management responsibility. All four regimes push sustainability issues into the boardroom.[249] EU directive incorporates sustainability duties into directors' responsibilities, the SEC explicitly requires disclosure of board oversight of climate risk, California's laws effectively pressure boards to ensure compliance with climate reporting (since non-compliance carries legal penalties), and the ISSB framework calls for disclosure on governance structures overseeing sustainability risks and opportunities, further reinforcing the expectation that boards play an active role in ESG oversight.[250]

Additionally, all frameworks encourage integrating sustainability into risk management. For example, SB 261 and the SEC rules both draw on the TCFD approach, which treats climate change as a core business risk to be identified and managed alongside other risks. The CSDDD similarly mandates a risk-based due diligence process for human rights and environmental harms. The CSRD requires companies to disclose sustainability-related risks and opportunities as part of their enterprise risk management and to align reporting with double materiality principles,

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[246] *See, e.g.,* DELOITTE & THE FLETCHER SCHOOL, *Investor Trust in Sustainability Data: Insights from the Global Investment Community* (Apr. 2024), https://www.eticanews.it/wp-content/uploads/2024/04/gx-global-report-investor-trust-in-sustainability-data.pdf; MCKINSEY & CO., *More Than Values: The Value-Based Sustainability Reporting That Investors Want*, https://www.mckinsey.com/capabilities/sustainability/our-insights/more-than-values-the-value-based-sustainability-reporting-that-investors-want (last visited Apr. 1, 2025).

[247] *See* WORLD ECON. F., *Why Sustainability Is Crucial for Corporate Strategy* (June 2022), https://www.weforum.org/stories/2022/06/why-sustainability-is-crucial-for-corporate-strategy (last visited Apr. 1, 2025).

[248] *See* GLOB. REPORTING INITIATIVE, *A Policymaker's Guide to Sustainability Reporting* (2023), https://www.globalreporting.org/media/nmmnwfsm/gri-policymakers-guide.pdf (last visited Apr. 1 , 2025).

[249] *See* Enriques, Gatti & Shapira, *supra* note 178.

[250] *Id.*

addressing both financial and impact risks, which is a much broader scope than the other regimes. The ISSB also places strong emphasis on governance and risk assessment as part of its IFRS S1 and S2 standards, reinforcing the need for companies to identify, assess, and manage material sustainability risks. This approach is making companies build internal accountability structures, like cross-functional sustainability committees, executive-level sustainability officers, and enhanced reporting lines to the board.[251]

Each framework also aims to combat "greenwashing" or insufficient action by requiring verification and enforcement. For instance, California and SEC rules require third-party assurance of climate data, while the CSRD similarly mandates third-party assurance of sustainability disclosures, moving from limited to reasonable assurance over time. The CSDDD includes both regulatory enforcement and the possibility of civil liability for companies that fail to meet their due diligence obligations. Although the ISSB does not impose enforcement mechanisms itself, many jurisdictions implementing its standards have indicated that assurance or supervisory oversight will be necessary.[252] This underscores a broader theme: sustainability matters are becoming enforceable compliance matters.

3.1.7. Key differences

One major difference among the regulations is the scope of issues covered. The SEC and California rules focus primarily on climate, with a goal to inform investors and the public about climate-related financial risks and carbon footprints. In contrast, the CSRD, CSDDD, and ISSB standards take a broader view, integrating social and governance elements such as labor practices and human rights due diligence. Among these, the CSDDD is particularly expansive: it imposes legal duties to prevent and mitigate adverse human rights and environmental impacts throughout global supply chains.[253]

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[251] *See* IFRS Found., *supra* note 22.

[252] *Id.*

[253] *See* EUROPEAN COMMISSION, *Corporate Sustainability Due Diligence Directive*, https://commission.europa.eu/business-economy-euro/doing-business-eu/sustainability-due-diligence-responsible-business/corporate-sustainability-due-diligence_en (last visited Aug. 2, 2025) (explaining CSDDD obligations and scope).

Another difference is mandatory action vs. disclosure. The SEC and SB 253/SB 261 are fundamentally disclosure-based regimes, despite controversies around them.[254] They do not tell companies how to reduce emissions or which risks to avoid; rather, they compel transparency, assuming that market pressures and public scrutiny will drive improvements. They require board-level oversight and third-party assurance, but generally stop short of requiring specific corporate behaviors or remedies. For example, SB 253 does not cap a company's emissions; it only requires measuring and reporting them. The CSRD, while also disclosure-driven, incorporates more hybrid features: it mandates double materiality and requires board sign-off on sustainability reports.[255] In contrast, the CSDDD mandates concrete changes in corporate behavior: companies must take action to prevent or end adverse impacts.[256] It is expressly prescriptive, requiring firms to remedy issues, such as supply chain labor violations, or to implement measures like a climate transition plan as part of compliance. This reflects a more interventionist European approach, grounded in protecting stakeholder rights, versus the U.S. approach, which leans on disclosure to influence investor behavior.[257]

The regulatory reach also differs. The SEC was designed to apply to all companies listed on U.S. stock exchanges, regardless of their country of incorporation, thus focusing on investor-owned corporations. California's laws apply to a broad range of large companies doing business in the state, including private companies and subsidiaries of foreign companies, an expansive reach but within one jurisdiction's economic footprint.[258] The EU directives have an international reach based on revenue criteria, effectively pulling international companies into the EU regulatory orbit

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[254] *See, e.g.,* EARTHJUSTICE, *Sierra Club, Earthjustice Challenge SEC's Weakened Climate Risk Disclosure Rule*, https://earthjustice.org/press/2024/sierra-club-earthjustice-challenge-secs-weakened-climate-risk-disclosure-rule (last visited Mar 14, 2024).

[255] *See* Clare Connellan et al., *Time to Get to Know Your Supply Chain: EU Adopts Corporate Sustainability Due Diligence Directive*, WHITE & CASE (July 5, 2024), https://www.whitecase.com/insight-alert/time-get-know-your-supply-chain-eu-adopts-corporate-sustainability-due-diligence-directive (last visited Jan. 7, 2025).

[256] *Id.*

[257] *See, e.g.,* Susan E. Dudley, *The U.S. and Europe Are Embarking on Dramatically Different Paths to Better Regulation*, GEO. WASH. U. REG. STUD. CTR. (Jan. 18, 2023), https://regulatorystudies.columbian.gwu.edu/us-and-europe-are-embarking-dramatically-different-paths-better-regulation; Hussein Dia, *Dancing to the Same Tune? EU and US Approaches to Standards*, 63 J. COMMON MKT. STUD. (2024), https://www.tandfonline.com/doi/full/10.1080/07036337.2024.2398430.

[258] *See* Olson, supra note 231.

if they want to access the European market. ISSB standards are being adopted by jurisdictions around the world, giving them a global regulatory reach.[259]

About enforcement mechanisms, U.S. frameworks (SEC and California) rely on regulators (SEC, CARB/AG) and the threat of penalties for non-compliance or material misstatements. According to the SEC rules, no longer in effect, the agency could have brought enforcement actions, and investors could have sued if disclosures were misleading, while California laws authorize annual fines for violations. The EU adds the powerful tool of civil litigation by outside stakeholders.[260] This means the liability risk profile under CSDDD is higher in some ways, as companies must worry about lawsuits from affected parties, not just regulatory fines. The ISSB does not impose enforcement mechanisms itself, but national regulators adopting its standards may do so.

Despite some differences, the shared features among these regimes underscore the emergence of a common governance architecture across jurisdictions—one that prioritizes board accountability, risk oversight, and internal controls. To illustrate this convergence, Table 1 compares the principal governance mechanisms in the EU, ISSB, SEC, and California frameworks.

Table 1. Governance Mechanisms Across Sustainability Regulations

Governance Mechanism	CSRD	CSDDD	SEC	California	ISSB
Board oversight of ESG risks	✓	✓	✓ (Limited to climate)	✓ (Implied, climate-focused)	✓
Board responsibility for strategy integration	✓	✓	✓ (Limited to climate)	✓	✓

[259] *See* IFRS FOUND., *IFRS Foundation Publishes Jurisdictional Profiles Providing Transparency and Evidencing Progress Toward Adoption of ISSB Standards*, IFRS News (June 12, 2025), https://www.ifrs.org/news-and-events/news/2025/06/ifrs-foundation-publishes-jurisdictional-profiles-issb-standards/ (last visited Jan. 12, 2025).

[260] *See* Baker McKenzie, supra note 169.

				(Implied, climate-focused)	
Executive accountability for ESG performance	✓	✓	✓	✓	✓
Financial risk materiality assessment & monitoring	✓	✓	✓	✓	✓
Integration of sustainability in financial reporting	✓	✗	✓	✗	✓
Use and disclosure of metrics and targets are recommended	✓	✓	✓	✓	✓
Internal controls/ processes for ESG data	✓	✓	✓	✓	✓
Mandatory climate risk disclosure	✓	✗	✓	✓	✓
Supply chain due diligence	✓	✓	✗	✗	✗
Climate transition plan required	✓	✓	✗	✗	✓ (Disclosure only)
Third-party assurance	✓	✗	✓ (Scopes 1 & 2)	✓ (Phased for Scope 3)	✗ (National discretion)
Civil liability for ESG-related harms	✓	✓	✗	✗	✗
Regulatory/legal penalties for non-compliance	✓	✓	✓	✓	✗ (National discretion)

4. Voluntary Drivers of Corporate Sustainability Governance

Voluntary ESG commitments are perceived as "soft law," aspirational and flexible in nature. But the reality is more complex. When a company voluntarily commits to disclosing greenhouse gas emissions under the GHG Protocol, incorporating science-based targets or reporting on environmental and social metrics, it must develop internal measurement systems, monitoring, and accountability.[261] Such choices, though not mandatory under law, usually lead to substantive governance shifts.[262] In this case, voluntary action is less a manifestation of good intentions; it is a catalyst for structural change.

This chapter explores how voluntary sustainability arrangements reshape corporate governance even in the absence of regulation. From the advent of voluntary reporting and the creation of board-level sustainability committees to the growing visibility of Chief Sustainability Officers (CSOs), from ESG-linked executive pay to Scope 3 supply chain stewardship, voluntary actions are transforming risk management and corporate decision-making. While there are still limitations in place, such as concerns around greenwashing,[263] uneven implementation and lack of enforcement, these initiatives have nonetheless laid the groundwork for a more strategic use of sustainability in the corporate sector.[264]

By examining these voluntary initiatives, this chapter complements the earlier analysis of regulatory developments, showing how voluntary sustainability efforts are likewise reshaping

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[261] *See* GHG PROTOCOL, *Standards & Guidance*, https://ghgprotocol.org/standards-guidance (last visited Jan. 12, 2025) (describing GHG Protocol as the world's most widely used greenhouse gas accounting standards, including the Corporate Standard, Scope 3 Standard, and other sector-specific tools).

[262] *Id.*

[263] *See* Peter Pears, Tim Baines, and Oliver Williams, *Greenwashing: Navigating the Risk*, HARV. L. SCH. F. ON CORP. GOVERNANCE (July 24, 2023), https://corpgov.law.harvard.edu/2023/07/24/greenwashing-navigating-the-risk/ (highlighting the reputational, regulatory, and litigation risks associated with greenwashing and emphasizing the need for accurate environmental disclosures).

[264] *See, e.g.*, CERES, *U.S. Securities and Exchange Commission Adopts Rule to Strengthen Fund Integrity and Market Confidence, Reduce Greenwashing* (Sept. 20, 2023), https://www.ceres.org/resources/news/u-s-securities-and-exchange-commission-adopts-rule-to-strengthen-fund-integrity-and-market-confidence-reduce-greenwashing (discussing how the SEC rules aimed at enhancing fund integrity and reducing greenwashing in investment products); OECD, *Due Diligence for Responsible Business Conduct* 19–23 (2018), https://mneguidelines.oecd.org/due-diligence-for-responsible-business-conduct.htm (last visited Aug. 12, 2025) (discussing uneven implementation and enforcement challenges in voluntary sustainability initiatives).

governance. Together, these forces illustrate the broader transformation of corporate governance into what this article terms corporate sustainability governance.

4.1. Voluntary Disclosure and the Rewiring of Governance

Voluntary sustainability disclosure guidelines are usually seen as instruments of transparency, but they are also potential drivers of governance reform. In embracing principles such as the GRI, the TCFD, or the Carbon Disclosure Project (CDP),[265] companies are not just disclosing information, but actually introducing new board-level obligations, risk management procedures, and internal controls into their system of governance.

Reporting on sustainability or ESG issues is almost a universal practice among major U.S. companies. A 2023 survey found that 100% of the Fortune 100 reported some data on sustainability in their SEC filings, and 93% of Russell 1000 companies published a standalone sustainability report.[266] Notably, all these figures keep rising over time, despite the recent ESG political and ideological backlash.[267] This indicates that despite the binding or nonbinding nature of these requirements, disclosure of sustainability has been a reality for companies.

Among the reporting standards, it is worth noting the role of the GRI, which has long been foundational, offering a comprehensive structure for companies to disclose their impacts across economic, environmental, and social issues. According to the 2024 KPMG Survey of Sustainability Reporting, 71% of the world's largest 5,800 companies use the GRI rules, an increase from 68% compared to 2022. GRI requires materiality tests, stakeholder consultation, and

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[265] *See* PERSEFONI, *CDP: Carbon Disclosure Project Beginner's Guide* (June 24, 2025), https://www.persefoni.com/blog/cdp-carbon-disclosure-project (last visited Aug. 2, 2025) (providing an overview of CDP as a voluntary international disclosure system where companies, cities, and investors can request environmental sustainability information).

[266] *See* GOVERNANCE & ACCOUNTABILITY INST., *2024 Sustainability Reporting in Focus* (Sept. 23, 2024), https://www.ga-institute.com/research/research/sustainability-reporting-trends/2024-sustainability-reporting-in-focus/ (last visited Jan. 7, 2025).

[267] *Id. See also* Ross Kerber, *Companies Boost Social and Climate Reporting Amid ESG Backlash*, REUTERS (Oct. 31, 2024), https://www.reuters.com/sustainability/companies-boost-social-climate-reporting-amid-esg-backlash-2024-10-31/ (last visited Apr. 1, 2025).

governance mechanisms, such as board-level oversight and executive accountability.[268] Generating a GRI-compliant report, thus, involves the necessity to adopt internal processes that usually involve legal, compliance, sustainability, and finance teams. This tends to prompt the establishment of cross-functional working groups and board committees charged with overseeing material factors and disclosure effectiveness. In this way, GRI not only promotes transparency but also formalizes sustainability monitoring in the organization.

The TCFD, the world's most widely used climate disclosure framework, places governance expectations even higher. Based on four pillars—governance, strategy, risk management, and metrics—the TCFD explicitly asks firms to detail how the board oversees climate-related risks and opportunities, and how management is involved in assessing and managing these risks.[269] Since the launch of the TCFD's recommendation report in 2017, nearly 5,000 companies in over 100 jurisdictions support the TCFD.[270] For most of them, aligning with these recommendations has required the board to formally assign responsibility for climate oversight, revise committee charters, and add climate risk to enterprise risk management frameworks.[271]

The CDP complements these frameworks by operating as a disclosure platform for environmental reporting. Companies that respond to CDP's annual climate questionnaires are evaluated not just on the completeness of their disclosures but on the strength of their governance structures, target-setting, and risk response mechanisms[272]. Because CDP scoring is used by

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[268] *See generally,* GLOBAL REPORTING INITIATIVE (GRI), *GRI 102: General Disclosures* 2016, at 22–23, https://www.globalreporting.org (last visited Mar. 7, 2025); For stakeholder engagement, *See* GLOBAL REPORTING INITIATIVE (GRI), *GRI 102: General Disclosures* 2016, at 24–25, https://www.globalreporting.org (last visited Mar. 7, 2025).

[269] *See* DELOITTE, *The TCFD's Four Pillars: Governance, Strategy, Risk Management, and Metrics & Targets*, *Deloitte Insights* (Feb. 2023), https://www.deloitte.com/ch/en/services/consulting-risk/perspectives/tcfd-and-why-does-it-matter.html (last visited Aug. 2, 2025) (noting the TCFD's 11 recommended climate-related disclosures are structured into four thematic areas: governance, strategy, risk management, and metrics and targets).

[270] *See* TASK FORCE ON CLIMATE-RELATED FIN. DISCLOSURES*, Final Report: Recommendations of the TCFD 2* (June 2017), https://www.fsb-tcfd.org/publications/final-recommendations-report/ (last visited Apr. 1, 2025).

[271] *See* TASK FORCE ON CLIMATE-RELATED FIN. DISCLOSURES, *Supporting the TCFD recommendations*, https://www.fsb-tcfd.org/ (last visited Aug. 2, 2025); TCFD Hub, *Governance* (describing how organizations align board and management responsibility, committee charters, and risk frameworks with TCFD guidance), https://www.tcfdhub.org/governance/ (last visited Aug. 2, 2025).

[272] *See* CDP, *CDP Climate Change 2023 Questionnaire: Guidance for Companies,* https://guidance.cdp.net/en/guidance?cid=46&ctype=theme&idtype=ThemeID&incchild=1&microsite=0&otype=Guidance&tags=TAG-13071%2CTAG-605%2CTAG-599 (last visited Apr. 6, 2025).

investors, companies may face reputational and market-based pressure to ensure high-quality reporting, which, in turn, leads many firms to develop better data systems, establish dedicated climate governance teams, and seek board involvement in emissions reduction strategies. Over 24,800 companies, representing two thirds of global market capitalization, report through CDP on climate change, forests and water security.[273] Notably, in response to investor expectations, many companies report under multiple standards simultaneously.[274]

The ISSB standards (IFRS S1 and S2), examined in the earlier section, are built based on TCFD and SASB frameworks to serve as a baseline for sustainability reporting with strong governance focus. They can be categorized as voluntary initiatives, since the ISSB itself has no compliance power, but they can also be mandatory as jurisdictions that adopt the rules decide so. For simplicity, this paper discussed IFRS S1 and S2 under the regulatory initiatives.[275]

In practice, adherence to voluntary disclosure standards is likely to compel firms to craft internal processes and controls for collecting and reporting sustainability data. However, the quality and rigor of voluntary disclosures can vary significantly across firms, depending on their internal capacity, corporate culture, and level of external pressure.[276] This unevenness raises concerns about the reliability and comparability of the information disclosed, potentially limiting its usefulness for investors and other stakeholders.[277] For this reason, several stakeholders, including academics, have called for regulatory mandates to establish consistent, enforceable standards for sustainability reporting.[278] Still, for many large corporations, especially those seeking to align with investor expectations, prepare for regulatory compliance or strengthen their position

[273] *See* CDP, *About Us*, https://www.cdp.net/en/about (last visited Apr. 1, 2025).

[274] *See* S&P GLOB., *Over 80% of Companies Using SASB Standards Also Report Under Other ESG Frameworks* (Nov. 10, 2021), https://www.spglobal.com/esg/insights/over-80-of-companies-using-sasb-standards-also-report-under-other-esg-frameworks (last visited Aug. 2, 2025) (finding that most companies use multiple ESG disclosure frameworks in parallel to meet diverse stakeholder and investor expectations).

[275] *See supra* Part 3.

[276] *See* Cynthia A. Williams & Jill E. Fisch, *Request for Rulemaking on Environmental, Social, and Governance (ESG) Disclosure*, 12 J. CORP. & SEC. L. 1 (2018), https://scholarship.law.upenn.edu/faculty_scholarship/1998.

[277] *Id.*

[278] *Id.*

in capital markets, these frameworks have the potential to drive meaningful upgrades to internal systems.

4.2. Boards, ESG Committees, and Director Expertise

One of the most concrete signs that voluntary sustainability commitments are reshaping corporate governance is the increasing embedding of board-level sustainability oversight. Companies have made this official by establishing dedicated board committees or expanding existing committee mandates. Companies reporting against frameworks like GRI, TCFD, and CDP are often asked to report on how their boards manage sustainability risks and opportunities, further advancing this trend.

In the early 2010s, few boards had explicit committees responsible for sustainability matters; today a strong majority do. In fact, a recent survey of Fortune 50 companies found 86% had a board-level committee overseeing ESG matters.[279] Many boards revised committee charters or created new committees in just the last few years: 83% of Fortune 50 firms updated their charters to bolster ESG oversight within a three-year span.[280] Broader analyses reinforce this trend. Within the Fortune 100, the number of firms that have a special ESG/sustainability board committee increased from as few as 22 to as many as 89 (of 100) from 2018 to 2023, pointing to the speed of institutionalization of sustainability governance.[281]

These committees, which can be part of or separate from audit, risk, or nominating committees, ensure that boards are thinking about sustainability issues on a regular basis within the context of risk management and company strategy.[282] Such committees also create clear reporting lines for management on sustainability performance and help signal to stakeholders that the company's leadership is monitoring sustainability targets at the highest levels. Governance

[279] *See* Lisa M. Fairfax, *Board Committee Charters and ESG Accountability*, COLUM. L. SCH.: BLUE SKY BLOG (Feb. 16, 2023), https://clsbluesky.law.columbia.edu/2023/02/16/board-committee-charters-and-esg-accountability/ (last visited Mar. 8, 2025).

[280] *See* Lisa Fairfax, *ESG's Death Defying Future: Predicting the Future of ESG Through the Lens of Current ESG Disclosure*, 26 U. PA. J. BUS. L. 1019 (2024), https://scholarship.law.upenn.edu/jbl/vol26/iss4/3..

[281] *See* Fairfax, *supra* note 279.

[282] *Id.*

experts note that integrating ESG into board committees makes oversight a "relatively permanent feature" of the board's role and not just a transitory topic.[283]

Recent political and market backlash against ESG has prompted some companies to rebrand, restructure, or broaden these committees under labels such as "sustainability," "responsible business," or "risk and opportunity."[284] While it is too soon to assess the long-term impact of these shifts, current evidence suggests that the underlying governance functions, integrating sustainability considerations into oversight and linking them to risk management and strategy, have so far persisted.[285] The backlash appears to have influenced terminology and framing more than the substantive role of sustainability governance, though future developments remain uncertain.[286]

To address these sustainability duties, boards have also begun professionalizing their sustainability oversight. This means that board members in most firms get sustainability training, ESG briefing, or even external learning on climate risk and human rights due diligence.[287] Some

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[283] *See* Matteo Tonello, *Sustainability in the Boardroom*, CONF. BD. (May 17, 2021), https://www.conference-board.org/blog/environmental-social-governance/Board-Sustainability-Oversight (last visited Aug. 12, 2025) (noting that embedding ESG in board committees makes sustainability oversight a "relatively permanent feature" of the board's responsibilities).

[284] *See* Andrew Watterson, *Addressing the ESG Backlash: It's Time to Explain the Why*, DIX & EATON (Oct. 4, 2023), https://www.dix-eaton.com/our-blog/addressing-the-esg-backlash-its-time-to-explain-the-why/ (last visited Aug. 9, 2025); *From Boom to Backlash: Guiding Directors in a Shifting ESG Landscape*, DIRECTORS & BOARDS (Jan. 9, 2024), https://www.directorsandboards.com/articles/from-boom-to-backlash-guiding-directors-in-a-shifting-esg-landscape/ (last visited Aug. 9, 2025); Patrick Temple-West, *Companies Drop 'ESG' Buzzword as Backlash Mounts*, FIN. TIMES (May 15, 2023), https://www.ft.com/content/43548347-8940-40e2-a557-c1e3c10d8f10 (last visited Aug. 9, 2025).

[285] *See Sustainability Under Scrutiny: 80% of Large Companies Adjust ESG Strategy Amid Political & Market Pressures*, CONFERENCE BOARD (Feb. 6, 2024), https://www.conference-board.org/press/sustainability-under-scrutiny-2025 (last visited Aug. 9, 2025).

[286] *See* Christine Short, *The Great ESG Rebrand: Why a Quieter Approach to Sustainability Is Winning*, WALL ST. HORIZON (Sept. 6, 2023), https://www.wallstreethorizon.com/blog/The-Great-ESG-Rebrand-Why-a-Quieter-Approach-to-Sustainability-Is-Winning (last visited Aug. 9, 2025).

[287] *See, e.g.,* PWC, *Comparing Board and C-Suite Perspectives on ESG* (2023), https://www.pwc.com/us/en/services/governance-insights-center/library/comparing-board-and-c-suite-perspectives.html (highlighting a disconnect between board and executive views on the importance of ESG expertise, with only 11% of directors rating it as "very important" compared to 57% of executives); Robert Walton, *Three Steps to Tackling the Green Skills Gap in the Boardroom*, REUTERS (Oct. 23, 2024), https://www.reuters.com/sustainability/boards-policy-regulation/comment-three-steps-tackling-green-skills-gap-boardroom-2024-10-23/ (last visited Aug. 9, 2025) (noting education programs such as climate governance designations to equip directors with sustainability competencies).

firms have sought to recruit directors with sustainability expertise, adding professionals with backgrounds in environmental science, social policy, or sustainability management to bring subject-matter knowledge to the boardroom.[288]

4.3. Executives, CSOs, and ESG-Linked Incentives

Voluntary sustainability commitments have made changes not just to board functions but also to executive accountability. With the rise of ESG, companies start to institutionalize sustainability through both structural leadership roles and incentive mechanisms, particularly by linking executive compensation to ESG performance.[289]

Many firms with sustainability practices now tie CEO and executive bonuses to sustainability performance metrics, such as carbon reduction targets, workplace diversity goals, or sustainable procurement benchmarks. A recent study shows that this practice has recently become more prevalent in U.S. public companies. Within S&P 500 firms during the 2023 proxy season, 315 of these firms (63.0%) included an ESG component in their executives' compensation and that the vast majority of these incentives are part of the annual incentive plan (AIA) rather than a part of the long-term incentive plan (LTIP).[290] The study also indicates that executives are more likely to achieve ESG goals than financial targets, with missed ESG targets predominantly occurring in areas with quantitative and standardized metrics, such as safety and emissions, which can suggest poor governance rather than a genuine commitment to sustainability objectives.[291] While concerns persist regarding the effectiveness and rigor of ESG-linked executive

[288] *See* Kristine Talbert, *Directors with Environmental and Social Credentials*, DIRECTORS & BOARDS (May 8, 2024), https://www.directorsandboards.com/board-issues/esg/report-the-percentage-of-directors-with-environmental-or-social-credentials-is-growing/ (last visited Aug. 9, 2025) (reporting the rise in board directors with environmental, governance, and social credentials between 2018 and 2023).

[289] *See Climate Metrics Surge in Executive Compensation Plans*, CONFERENCE BOARD (Jan. 4, 2024), https://www.conference-board.org/press/ESG-metrics-in-exec-comp-2024 (last visited Aug. 9, 2025) (noting climate-related metrics in executive compensation rose from 25% of S&P 500 firms in 2021 to 54% in 2023).

[290] *See* Badawi & Bartlett, *supra* note 69.

[291] *Id.*

compensation, the broader trend is undeniable: many large companies have altered this governance mechanism to include these new concerns.

In parallel, some businesses have created new executive roles to manage sustainability strategies and compliance. The most prominent of these is the Chief Sustainability Officer (CSO). While still not highly prevalent—fewer than 200 U.S. public companies had a CSO as of 2022—[292] the position is growing more influential in multinational giants. CSOs typically have the responsibility to map internal practices against external benchmarks such as TCFD or CDP and align different teams inside the company to collect, validate, and report data. In addition, CSOs generally report to the CEO, CFO, or to the board directly, proof of the strategic importance of their role.[293] However, the relatively limited adoption of the CSO role indicates that many firms yet rely on informal committees or delegate sustainability responsibilities to other senior leaders, such as general counsel or heads of strategy.[294] At the same time, the recent backlash against ESG has prompted some companies to reconsider how these roles are titled or framed, with certain firms opting for alternative labels such as "chief impact officer" or "head of corporate responsibility" to defuse political criticism while maintaining the underlying strategic functions.[295]

Beyond compensation and leadership roles, accountability has also increased through companies' alignment with external voluntary frameworks that demand structural governance changes. One of the most prominent is the Greenhouse Gas (GHG) Protocol, a globally recognized framework and set of standards, developed by the World Resources Institute (WRI)[296] and the

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[292] *See* Ellen Weinreb, *The Communication Woes of CSOs*, HOWER IMPACT (last visited Mar. 8, 2025), https://howerimpact.com/thesustainabilitycommunicator/ep-15-the-communication-woes-of-csos-with-ellen-weinreb; Yusuf Khan, *Sustainability Chiefs Say Their Roles Have Become More Complex and Relevant*, WALL ST. J. (May 22, 2024) (noting U.S. public companies rose from 29 to roughly 183 CSOs between 2011 and 2022); *Banks Downgrade Top Sustainability Roles*, FIN. TIMES (Mar. 2025) (reporting some banks have downgraded sustainability roles amid political backlash).

[293] *See* PEOPLEASSET, *The Rising Importance of the Chief Sustainability Officer* (last visited Mar. 8, 2025), https://peopleasset.in/knowledge-and-resources/blogs/the-rising-importance-of-the-chief-sustainability-officer/.

[294] *Id.*

[295] *See* Khan, *supra* note 292.

[296] *See* WORLD RES. INST. & WORLD BUS. COUNCIL FOR SUSTAINABLE DEV., *The Greenhouse Gas Protocol: A Corporate Accounting and Reporting Standard* (rev. ed. 2004), https://ghgprotocol.org/sites/default/files/standards/ghg-protocol-revised.pdf.

World Business Council for Sustainable Development (WBCSD),[297] for measuring, managing, and reporting greenhouse gas emissions. It provides tools and guidance for businesses, governments, and other organizations to measure and report their carbon footprint. Well before regulatory mandates, many companies had already committed to the GHG Protocol and constructed internal procedures to collect and validate emissions data.[298] Organizations that report according to the GHG Protocol also must put in place governance arrangements that enable good emissions reporting, board-level approval of climate plans, and third-party assurance of reported data.[299]

Similarly, companies adopting the Science-Based Targets Initiative (SBTi) must ensure that their boards and executive teams oversee emission reduction targets, reinforcing sustainability as a strategic business concern. Although companies can withdraw their commitment to measuring carbon emissions or setting targets at any time—and some already did—[300] dismantling the governance structures established for this purpose is unlikely, or at the very least, a complex and challenging task. There are processes and controls in place and, once integrated, these frameworks become incorporated in corporate risk management, compliance, and reporting systems, making their complete removal disruptive to internal operations and stakeholder expectations.

4.4. Internal Architecture: Controls and Data Systems

Meeting voluntary sustainability commitments often necessitates the creation of an internal architecture capable of producing reliable, consistent, and auditable sustainability data, particularly in relation to environmental matters.[301] As companies pledge to reduce emissions, announce net-

[297] *See* WORLD RES. INST. & WORLD BUS. COUNCIL FOR SUSTAINABLE DEV., *About Us*, GHG Protocol, https://ghgprotocol.org/about-us (last visited Feb. 4, 2025).

[298] *See* Gadinis, *supra* note 97.

[299] *See* SCI. BASED TARGETS INITIATIVE, *Foundations for Science-Based Net-Zero Target Setting in the Corporate Sector* (Oct. 2021), https://sciencebasedtargets.org/resources/files/foundations-for-net-zero-full-paper.pdf.

[300] *See, e.g.,* Kenza Bryan & Attracta Mooney, *How Companies Are Starting to Back Away from Green Targets*, FIN. TIMES (June 20, 2024), https://www.ft.com/content/c9fee776-1471-442c-aae8-8d78fe60faeb (reporting on a growing trend of corporations quietly scaling back environmental targets amid political backlash and shifting investor pressure).

[301] *See* Robert Kammerer et al., *Internal Controls: Building Sustainability Reporting on Strong Foundations*, PWC (Dec. 20, 2024), https://www.pwc.com/gx/en/services/audit-assurance/corporate-reporting/esg-

zero targets, or report Scope 3 emissions, they are under mounting pressure to develop internal controls and auditing procedures similar to those used in financial reporting.[302] Internal controls over sustainability data, including control mechanisms akin to those used for financial disclosure, are essential to ensure data accuracy, credibility, and audit readiness amid growing regulatory mandates and stakeholder scrutiny.[303]

Commitments under the GHG Protocol and the SBTi, for example, imply that firms will measure and report emissions, what can happen across different Scopes (1, 2 and 3) and geographies.[304] These disclosures are dynamic; they must be updated annually, on the basis of underlying operational data from the business itself or form its value chain. This, in turn, has led many firms to invest in comprehensive data management processes that require input not just from inside but also from outside stakeholders, such as subsidiaries and suppliers.[305]

Perhaps the best evidence that voluntary climate commitments need robust governance systems is the challenge of measuring and managing Scope 3 emissions, which involves indirect emissions generated across a company's entire value chain.[306] They are often the largest share of a firm's carbon footprint but the most difficult to measure and control.[307] The record number of public comment letters submitted to the SEC during its climate disclosure rulemaking between 2022 and

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reporting/internal-controls-on-strong-foundations.html (last visited Aug. 9, 2025) (discussing how principles from financial reporting control environments carry over to ensure credibility and reliability in sustainability reporting).

[302] *Id.*

[303] *See* DELOITTE, *Using the COSO Framework to Establish Internal Controls Over Sustainability Reporting (ICSR)*, (Apr. 21, 2023), https://dart.deloitte.com/USDART/home/publications/deloitte/heads-up/2023/coso-framework-for-internal-controls-over-sustainability (last visited Aug. 9, 2025) (highlighting COSO's recent guidance on applying established internal control frameworks to ESG reporting).

[304] It is worth noting, however, that the Protocol was not designed as an "all-or-nothing" standard, allowing companies significant flexibility to apply only selected parts. *See generally* Jessica F. Green, *Private Standards in the Climate Regime: The Greenhouse Gas Protocol*, 12 BUS. & POL. 1 (2010) (explaining how companies were instrumental to develop the GHG Protocol).

[305] *See* Gadinis, *supra* note 97.

[306] *See* Maximilian Hettler & Lorenz Graf-Vlachy, *Corporate Scope 3 Carbon Emission Reporting as an Enabler of Supply Chain Decarbonization: A Systematic Review and Comprehensive Research Agenda*, BUSINESS STRATEGY AND THE ENVIRONMENT, https://onlinelibrary.wiley.com/doi/abs/10.1002/bse.3486 (last visited Feb 2, 2024).

[307] *See* U.S. ENVTL. PROT. AGENCY, *Scope 3 Inventory Guidance*, https://www.epa.gov/climateleadership/scope-3-inventory-guidance (last visited Apr. 1, 2025).

2024 illustrate that nuance.[308] Scope 3 disclosure was the most debated of all requirements,[309] with many companies urging caution or exemptions on the grounds that supplier and customer data are difficult to verify and would involve a complex and expensive governance process.[310] This resistance points to a key fact that Scope 3 emission measurement and reduction require not only environmental aspiration, but enormous governance infrastructure, from data management and supplier engagement to assurance and legal oversight.[311]

Despite these challenges—and the fact that the SEC ultimately dropped its proposed Scope 3 disclosure requirement[312]—several leading U.S. companies are nonetheless establishing governance structures to support Scope 3 measurement and emissions reduction. For instance, AT&T met its Scope 3 science-based target two years ahead of schedule by partnering with suppliers accounting for 53% of its entire spending to adopt their own science-based emissions targets.[313] McDonald's has collaborated with suppliers using methane-reducing cattle feed, such as genetically modified Enogen corn, to help lower agricultural emissions, as part of its broader push

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[308] *See* Lawrence A. Cunningham, *What the Volume and Diversity of Comment Letters to the SEC Say About Its Climate Proposal*, HARV. L. SCH. F. ON CORP. GOVERNANCE (July 3, 2022), https://corpgov.law.harvard.edu/2022/07/03/what-the-volume-and-diversity-of-comment-letters-to-the-sec-say-about-its-climate-proposal/.

[309] *See, e.g.,*, Jacob H. Hupart, *SEC Expected to Drop Scope 3 GHG Emissions Disclosure Requirements from Final Climate Rule*, NAT'L L. REV. (Feb. 26, 2024), https://natlawreview.com/article/sec-expected-drop-scope-3-ghg-emissions-disclosure-requirements-final-climate-rule (last visited Feb. 6, 2025) (explaining the opposition faced by the SEC concerning its proposed Scope 3 emissions disclosure requirements, leading to the decision to drop the mandate).

[310] *See, e.g.,* Evan Williams, *The Chamber Fights Back Against Counterproductive Corporate Disclosure Requirements*, U.S. CHAMBER OF COMMERCE (Jan. 30, 2024), https://www.uschamber.com/finance/corporate-governance/the-chamber-fights-back-against-counterproductive-corporate-disclosure-requirements (last visited Feb. 6, 2025); *See* NAT'L ASS'N OF MFRS., *Comment Letter on SEC Proposed Rule: The Enhancement and Standardization of Climate-Related Disclosures for Investors* (June 17, 2022), https://documents.nam.org/tax/nam_comments_sec_climate_rule.pdf (last visited Feb. 6, 2025); BUSINESS ROUNDTABLE, *Comment Letter on SEC Proposed Rule: The Enhancement and Standardization of Climate-Related Disclosures for Investors* (June 17, 2022), https://s3.amazonaws.com/brt.org/2022.06.17-BRT.Countryman.TheEnhancementandStandardizationofClimate-RelatedDisclosuresforInvestors3.pdf (last visited Feb. 6, 2025) (emphasizing the challenges of gathering reliable supply chain data and warning about compliance burdens).

[311] *Id.*

[312] *See, e.g.*, Zoya Mirza & Lamar Johnson, *Conflicting Views on SEC's Authority Set the Tone for Climate Disclosure Rule Vote*, ESG DIVE (Mar. 7, 2024), https://www.esgdive.com/news/sec-climate-disclosure-rule-vote-recap-commissioners-disagree-on-authority/709643/ (last visited Feb. 6, 2025).

[313] *See* AT&T, *Climate & Emissions*, https://sustainability.att.com/priority-topics/climate-change-ghg (last visited Apr. 1, 2025).

to achieve net-zero by 2050 and halve its restaurant and office emissions by 2030.[314] Walmart, through its Project Gigaton, has enlisted its own thousands of suppliers to track and reduce emissions, including offering tools and even special financing in order to facilitate sustainable practices in its worldwide value chain.[315] These efforts require companies not just to collect information, but to create contractual, technological, and strategic frameworks that embed sustainability in supply chain management.[316] Moreover, these initiatives generate a "cascading governance effect": when large firms commit to reporting Scope 3 emissions, they, in effect, push governance demands down the supply chain.

4.5. The Fragility of Voluntarism: Greenwashing and Backlash

Though voluntary sustainability initiatives have prompted valuable corporate governance reforms, they also create cynicism. Among these is the phenomenon of "greenwashing," where companies pledge to make sustainability reforms but end up making only cosmetic or superficial changes.[317] It is relatively easy for firms to publish visually impressive sustainability reports or announce pledges like "net-zero by 2050" without altering their core business models. In some cases, companies have even begun reversing emissions reduction targets after deciding that their earlier targets had been committed to without a viable plan for execution. [318]

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[314] *See* SYNGENTA, *McDonald's USA, Syngenta & Lopez Foods Collaborate to Help Produce Beef More Sustainably in the US* (Nov. 14, 2024), https://www.syngenta.com/media/media-releases/2024/mcdonalds-usa-syngenta-and-lopez-foods-collaborate-help-produce-beef-more (last visited Mar. 10, 2025).

[315] *See* WALMART INC., *Walmart Suppliers Lead the Charge, Help Deliver Project Gigaton Goal More Than Six Years Early*, https://corporate.walmart.com/news/2024/02/21/walmart-suppliers-lead-the-charge-help-deliver-project-gigaton-goal-more-than-six-years-early (last visited Apr. 1, 2025).

[316] *See, e.g,* Mark Segal, *Salesforce Adds Climate Obligations to All Supplier Contracts*, ESG TODAY (Apr. 29, 2021), https://www.esgtoday.com/salesforce-adds-climate-obligations-to-all-supplier-contracts/ (last visited Dec. 2, 2024) (explaining that the company incorporated groundbreaking addition to supplier contracts creating legally binding obligations for climate action).

[317] *See* SV de Freitas Netto et al., *Concepts and Forms of Greenwashing: A Systematic Review*, 10 ENVIRON. SCI. EUR. 1, 3–4 (2020) (defining greenwashing as misleading environmental performance claims and noting its proliferation), https://enveurope.springeropen.com/articles/10.1186/s12302-020-0300-3 (last visited Aug. 9, 2025).

[318] *See* Kenneth P. Pucker, *Companies Are Scaling Back Sustainability Pledges. Here's What They Should Do Instead,* HARV. BUS. REV. (Aug. 20, 2024), https://hbr.org/2024/08/companies-are-scaling-back-sustainability-pledges-heres-what-they-should-do-instead (last visited Apr. 1, 2025).

The main point is that voluntary commitments lack enforceability. Companies can make 2050 net-zero commitments, adopt human rights guidelines, or utilize disclosure frameworks, but without third-party validation or the risk of legal action, nobody can be certain they will follow through. While there are thousands of companies who support the TCFD, analysis has revealed many examples where they don't provide the extent of or quality of disclosure the framework envisions.[319]

This dynamic was visible in the aftermath of the 2019 Business Roundtable statement, in which more than 180 CEOs pledged to serve all stakeholders, not just shareholders.[320] The statement was considered as a paradigm shift in corporate purpose, but subsequent research showed that few of the signatories made actual governance adjustments—such as amending their corporate charters or decision-making frameworks—to underpin this new stakeholder emphasis.[321] Professors Lucian Bebchuk and Roberto Tallarita famously branded the statement as an "illusory promise," warning that symbolic stakeholderism would undermine accountability by defending management from shareholder oversight.[322] In other words, the risk is that voluntary sustainability governance may supplant genuine reform, creating the illusion of sustainability without changing underlying structures. This can be particularly problematic when companies use these credentials to attract investors, customers, or talents, without meaningfully improving environmental or social outcomes.

Empirical research on this area produces mixed results. Some find that firms with intense ESG monitoring, such as dedicated board committees or third-party assurance, have better sustainability performance.[323] Others observe little correlation between institutionalized ESG plans and results, suggesting procedural reform will not suffice unless supplemented by substantive

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[319] *See* Alix Auzepy et al., *Evaluating TCFD Reporting—A New Application of Zero-Shot Analysis to Climate-Related Financial Disclosures*, 18 PLOS ONE E0288052 (2023), https://doi.org/10.1371/journal.pone.0288052.

[320] *See* Business Roundtable, *supra* note 310.

[321] *See*. Bebchuk & Tallarita, *supra* note 6.

[322] *Id.*

[323] *See* Yunice Karina Tumewang et al., *Sustainability Committee, External Assurance, and ESG Performance: Empirical Evidence from Banking Industry in Emerging Economies*, 32 CORP. SOC. RESP. & ENV'T MGMT. 2728 (2025), https://doi.org/10.1002/csr.3095; Alfonso Del Giudice & Silvia Rigamonti, *Does Audit Improve the Quality of ESG Scores? Evidence from Corporate Misconduct*, 12 SUSTAINABILITY 5670 (2020), https://doi.org/10.3390/su12145670.

engagement or incentives.[324] Also, variations in ESG ratings and measures pose a problem for investors to compare businesses or verify voluntary statements, prompting calls for unified disclosure standards and stronger investor stewardship to complement voluntary schemes.[325] Even some business CEOs now believe that required reporting rules will level the playing field and restore credibility to sustainability reporting.[326]

In general, while voluntary sustainability efforts have stimulated meaningful reforms, their effectiveness depends on the level and openness of governance and third-party review. Advocates argue that they have introduced new structures, such as new committees, sustainability officers, and external assurance, and placed climate and society issues at board and executive attention.[327] Critics caution that without external accountability, voluntary initiatives will be inclined to act as reputation management systems rather than sources of deeply ingrained change.[328] The reality likely lies somewhere in between: voluntary sustainability initiatives have come a long way, bringing matters like climate and human capital to boards' agendas, but making sure they are producing concrete outcomes is the next governance challenge. Meeting that test will require sustained pressure from investors, regulators, and other stakeholders, along with more transparent standards and rigorous monitoring to distinguish genuine progress from performative action.

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[324] *See* Abdullah et al., *Sustainable Development: The Role of Sustainability Committees in Achieving ESG Targets*, 33 BUS. STRATEGY & ENV'T 2250 (2024), https://doi.org/10.1002/bse.3596 (finding that while certain committee characteristics may influence governance scores positively, their overall effectiveness in enhancing sustainability performance varies).

[325] *See* Paul Verney, *RI Stewardship Survey: 57% of Investors Back Mandatory Stewardship Disclosures*, RESPONSIBLE INVESTOR (May 29, 2024), https://www.responsible-investor.com/ri-stewardship-survey-57-of-investors-back-mandatory-stewardship-disclosures/

[326] *See, e.g.,* Joe Allanson, *Why Salesforce Is Urging Corporations to Support the SEC's Climate Disclosure Rule*, SALESFORCE NEWS & INSIGHTS (June 15, 2022), https://www.salesforce.com/news/stories/why-salesforce-is-urging-corporations-to-support-the-secs-climate-disclosure-rule/. Patrick Temple-West, *Corporate Leaders Call for Mandatory ESG Reporting to Boost Credibility*, FIN. TIMES (Nov. 12, 2023), https://www.ft.com/content/f2b6d38e-68d5-4a5d-bd2e-b0dc91b6e7f0 (last visited Aug. 9, 2025).

[327] *See* Robert G. Eccles, Mary Johnstone-Louis, Colin Mayer & Judith C. Stroehle, The Board's Role in Sustainability, Harv. Bus. Rev., Sept.–Oct. 2020, https://hbr.org/2020/09/the-boards-role-in-sustainability (last visited Jan. 12, 2025) (arguing that voluntary ESG efforts have spurred changes, including the creation of new board committees, appointment of sustainability officers, and use of external assurance to integrate sustainability into board oversight).

[328] *See* Michael P. Vandenbergh, *Private Environmental Governance*, 99 CORNELL L. REV. 129, 167–69 (2013) (arguing that without binding rules, voluntary programs often serve reputational purposes more than substantive reform).

5. Toward a New Model: The Emergence of Corporate Sustainability Governance

As discussed in previous sections, both voluntary and regulatory regimes increasingly require new substantive structures and processes of governance from corporations. These regimes converge on the main governance expectations: board-level oversight of sustainability matters, executive accountability, internal controls over sustainability information, mechanisms for stakeholder engagement, and periodic disclosures. Convergence has laid the groundwork for a new governance regime, that this article has referred to as corporate sustainability governance. It is neither entirely voluntary nor solely regulatory, but a hybrid system founded on accountability, transparency, and risk management.

This chapter explores the ways in which sustainability governance has reshaped traditional corporate governance structures. It focuses on the new roles for executives and boards, emerging risk management frameworks, evolving fiduciary obligations, and the incorporation of sustainability into corporate decision-making. Taken together, these shifts have established a hybrid form of corporate governance that weighs financial and non-financial performance metrics, changing the manner in which companies think about long-term value. Even in light of regulatory uncertainties and political backlashes mount, the governance transition underway appears structural, rather than episodic.

5.1. Agency Theory and Board Accountability

Corporate sustainability governance has broadened classical board accountability by adding environmental and social oversight to the central responsibilities of the board. While traditional corporate governance has concentrated its attention on financial matters, recent sustainability regulations as well as voluntary initiatives encourage board engagement with many other concerns, including climate change, human rights, and broader sustainability threats.

On the regulatory side, instruments such as the EU's CSRD and CSDDD, ISSB standards, SEC Climate Disclosure Rules, and California climate rules have all cumulatively redefined the board's role in overseeing sustainability risks. While the SEC and California rules specifically deal with climate-related risks, the CSRD, CSDDD and ISSB expand the scope of oversight to broader environmental and social effects.[329] For example, the CSRD requires boards to publish board-approved sustainability statements and the CSDDD imposes due diligence obligations that make directors accountable for identifying and mitigating sustainability risks in the value chain. While these reforms enhance disclosure, they also provide a foundation for legal accountability when harm arises from sustainability issues.

Voluntary strategies also demand board accountability. Companies committed to frameworks such as the TCFD and the GHG Protocol must incorporate board oversight on climate risk and emission reports. Similarly, GRI and ISSB standards demand disclosure on how boards manage sustainability and evaluate progress for performance metrics. Companies that make public disclosure of sustainability objectives—especially those that place such information in financial reports or get third-party assurance—are effectively binding their boards to these performance goals.

In reality, firms that fall under these regulatory regimes or have voluntarily tied themselves to these initiatives need to put in place governance structures to enable these commitments.[330] Others have even gone further by establishing board-level ESG or sustainability committees, bolstering the principle that these kinds of risks need to be addressed and monitored similarly to financial risks.[331] Moreover, by releasing information regarding climate goals, working conditions,

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[329] The ISSB is also developing new standards that may expand the scope of social and environmental disclosures. *See* IFRS FOUND., *ISSB Update — July 2025*, https://www.ifrs.org/news-and-events/updates/issb/2025/issb-update-july-2025 (last visited Aug. 12, 2025) (highlighting research projects on biodiversity, ecosystems, and human capital included in the ISSB's work plan agenda).

[330] *See* Tensie Whelan & Caroline Flammer, *Corporate Governance and Sustainability: A Framework for Board Oversight*, HARV. L. SCH. F. ON CORP. GOVERNANCE (Oct. 25, 2021), https://corpgov.law.harvard.edu/2021/10/25/corporate-governance-and-sustainability-a-framework-for-board-oversight/ (last visited Aug. 9, 2025) (explaining that meeting sustainability commitments requires specific governance structures and oversight mechanisms).

[331] *See* Eccles et. al, *supra* note 327 (noting the rise of board-level ESG committees and their role in treating sustainability risks alongside financial risks). *See also* ROBERT G. ECCLES & MICHAEL P. KRZUS, *ONE REPORT: INTEGRATED REPORTING FOR A SUSTAINABLE STRATEGY* (John Wiley & Sons 2010).

or supply chains, such companies are expanding their accountability beyond shareholders and toward a more universal group of stakeholders.[332]

Rather than undermining accountability, sustainability governance restates it. Boards remain accountable for the traditional fiduciary duties but now encompass a wider risk list, including financially material sustainability risks.[333] Thus, this reorientation does not dilute governance discipline but demands even more formalized scrutiny, strengthened internal controls, and more transparent public disclosure, so that sustainability vigilance is actionable and transparent.[334]

5.2. Executive Involvement and Incentives

The emergence of the corporate sustainability governance has reshaped executive roles and incentives by merging environmental and social objectives into core management tasks. While traditional corporate governance confined executive responsibility to financial performance and shareholder return,[335] modern governance compels senior executives to take at least some environmental and social considerations into account when making business decisions.

Several disclosure regimes explicitly require executive-level engagement with sustainability risks and reporting. Under the CSRD, firms must disclose how their management bodies are involved in the oversight of sustainability matters and approval of related statements.

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[332] *See* Larry Fink, *A Fundamental Reshaping of Finance*, BLACKROCK (Jan. 14, 2020), https://www.blackrock.com/corporate/investor-relations/2020-larry-fink-ceo-letter (last visited Aug. 9, 2025) (arguing that corporate disclosure on issues like climate change and workforce practices reflects a shift toward broader stakeholder accountability).

[333] *See* BDO, *Understanding the Board's ESG Mandate* (Nov. 14, 2022), https://www.bdo.com/insights/assurance/understanding-the-boards-esg-mandate (last visited Aug. 2, 2025) (explaining that boards' traditional duties of care and loyalty already encompass ESG, meaning that as sustainability risks become more material, boards must address those risks alongside financial concerns).

[334] *See* Robert G. Eccles, Ioannis Ioannou & George Serafeim, *The Impact of Corporate Sustainability on Organizational Processes and Performance*, 60 MGMT. SCI. 2835, 2838–40 (2014), https://www.hbs.edu/ris/Publication%20Files/SSRN-id1964011_6791edac-7daa-4603-a220-4a0c6c7a3f7a.pdf.

[335] *See* Stout, *supra* note 43 (describing how the shareholder primacy model historically framed corporate purpose in terms of financial returns to shareholders); Andrew Edgecliffe-Johnson, *Boards Face Pressure to Look Beyond Shareholder Value*, FIN. TIMES (Mar. 3, 2022), https://www.ft.com/content/1b2a3dc5-24a7-41e0-89e4-5d7cbfa9931b (last visited Aug. 9, 2025) (observing that traditional governance was largely focused on shareholder value maximization).

The ISSB's IFRS S1 and S2 likewise require companies to disclose the governance processes, controls, and procedures used by management to monitor and oversee sustainability-related and climate-related risks and opportunities. Similarly, California climate laws require disclosure of the leaders and infrastructure used to measure emissions and monitor climate-related financial risks. Even on a voluntary basis, TCFD ask firms to specify the role of management in assessing and managing risks. As a result, CEOs, CFOs, general counsels, and risk officers have more accountability to ensure compliance, accuracy, and completeness of sustainability information and disclosures.

Along with compliance, sustainability initiatives are also shaping executive compensation systems. Most major companies linked executive pay to emission reduction goals, workplace safety and diversity, among others sustainability matters. By linking executive compensation to target sustainability measures, corporations convey to stakeholders that progress is leadership's responsibility in direct terms.

Finally, while not yet widespread, the creation of CSO roles evidences a further institutionalization of sustainability governance through corporate leadership. While in the past firms created novel C-suite positions based on strategic demands,[336] now they appoint CSO as a result of a combination of market force, regulatory shifts, and reputation risk. Regulations like the CSDDD directive reinforce this trend by requiring board-level and management-level sustainability expertise.[337] Having a CSO can be of specific value for companies with science-based targets or complicated value chains, where internal coordination and technical expertise are a priority.

[336] *See* Dirk M. Zorn, *Here a Chief, There a Chief: The Rise of the CFO in the American Firm*, 69 AM. SOC. REV. 345 (2004), https://doi-org.libproxy.berkeley.edu/10.1177/000312240406900302.

[337] *See* Clifford Chance, *Corporate Sustainability Due Diligence Directive: Key Requirements for Boards and Management* (Mar. 20, 2024), https://www.cliffordchance.com/insights/resources/blogs/business-and-human-rights/2024/03/csddd-key-requirements.html (last visited Aug. 9, 2025) (explaining the governance expertise provisions and implications for corporate boards).

5.3. Risk Management and Control Systems

Corporate sustainability governance has also significantly changed risk management systems by embedding environmental and social risks in the very center of these functions. Traditionally, corporate governance considered risk management as an essential financial activity, with executives and boards worrying about market, credit, or operational risk.[338] However, new regulatory and voluntary norms now force businesses to identify, assess, and manage a broad spectrum of risks, such as climate, environmental, and human rights risks, that were previously considered non-financial or secondary.

Under the SEC rule, California's SB 261, and the EU's CSRD/ESRS, companies must disclose material climate risks and describe the governance and risk-management processes used to address them, placing these matters under direct board and executive oversight. These regulations require disclosure of physical risks (e.g., intense weather conditions, droughts, floods) and transition risks (e.g., policy changes, carbon pricing, shifts in consumer preferences) and how such risks influence the company's financial outlook and strategy.[339] Most importantly, disclosures must explain the systems of governance in place to manage these issues, subjecting risk management to greater transparency and scrutiny at the highest corporate levels.

The CSDDD introduces an even wider conception of risk, asking firms to perform due diligence on everything they do and in their supply chains.[340] Firms must identify, prevent, and mitigate adverse impacts on human rights and the environment in their own operations, in their

[338] *See* WORLD ECON. F., *Global Risks Report 2024* 7–10 (2024), https://www.weforum.org/reports/global-risks-report-2024/ (last visited Aug. 9, 2025) (noting the integration of environmental and social risks into enterprise risk management and contrasting this with traditional market, credit, and operational risk focus).

[339] *See* TCFD, *supra* note 13 (defining "physical risks" as those arising from acute weather events or chronic climate patterns and "transition risks" as those associated with policy, legal, technological, and market changes aimed at reducing greenhouse gas emissions); DELOITTE, *Understanding Physical and Transition Risks in Climate Reporting* (Feb. 2023), https://www2.deloitte.com/global/en/pages/risk/articles/understanding-physical-and-transition-risks.html (last visited Aug. 9, 2025) (summarizing how these risk categories are used in global climate disclosure frameworks).

[340] *See* WHITE & CASE, *EU's Corporate Sustainability Due Diligence Directive (CSDDD): What Companies Need to Know* (Jan. 12, 2024), https://www.whitecase.com/insight-alert/eus-corporate-sustainability-reporting-directive-and-esrs-what-companies-need-know (last visited Aug. 9, 2025) (explaining that the CSDDD mandates due diligence throughout operations, subsidiaries, and the chain of activities).

subsidiaries, and suppliers.[341] This involves the implementation of effective internal controls, supplier engagement, grievance mechanisms, and remediation.[342] The risk management function is no longer limited to intra-corporate activities; it now extends to third-party relationships, most notably through Tier 1 suppliers and potentially further.

Voluntary action has also institutionalized sustainability risk management. For example, TCFD encourages companies to adopt forward-looking scenario analysis to estimate business model resilience to various climatic futures. GHG Protocol and SBTi also require companies to measure and reduce their carbon footprints, which involve extensive value chain mapping and engagement. In parallel, companies doing social supply chain due diligence must at least establish risk mapping procedures.[343] Taken together, these requirements have prompted companies to develop sophisticated risk assessments and materiality evaluations of sustainability, many of which are reviewed by boards or specific committees.

The integration of sustainability into risk management processes has also transformed internal compliance and control systems. Companies are establishing cross-functional teams of legal, compliance, sustainability, finance, and procurement departments to ensure that sustainability risks are tracked and managed.[344] Some companies have established ESG-specific dashboards and key risk indicators (KRIs), and others conduct regular sustainability audits or ask

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[341] *See* MAYER BROWN, *Human Rights and the Environment: What to Expect from the Corporate Sustainability Due Diligence Directive* (Mar. 19, 2024), https://www.mayerbrown.com/en/insights/publications/2024/03/human-rights-and-the-environment--what-to-expect-from-the-corporate-sustainability-due-diligence-directive (last visited Aug. 9, 2025) (outlining requirements to integrate due diligence into management systems, conduct risk mapping, and establish grievance mechanisms).

[342] REUTERS, *EU Parliament Approves New Business Supply-Chain Audit Law* (Apr. 24, 2024), https://www.reuters.com/world/europe/eu-parliament-approves-new-business-supply-chain-audit-law-2024-04-24/ (last visited Aug. 9, 2025) ("compelling larger companies… to audit their supply chains for forced labour and environmental damage" and "act on their findings," extending responsibility to upstream and downstream partners).

[343] *See* SCI. BASED TARGETS INITIATIVE, *SBTi Criteria and Recommendations* 9–12 (Apr. 2023), https://sciencebasedtargets.org/resources/files/SBTi-criteria.pdf (last visited Aug. 9, 2025) (requiring measurement and reduction of value chain emissions for target validation).

[344] *See* DELOITTE, *Integrating ESG into Enterprise Risk Management* 4–6 (2023), https://www2.deloitte.com/global/en/pages/risk/articles/esg-in-enterprise-risk-management.html (last visited Aug. 9, 2025) (explaining that cross-functional teams are critical to embedding ESG in ERM and ensuring data quality).

for third-party assurance of sustainability data to improve credibility and compliance.[345] As sustainability becomes incorporated into the corporation's control systems, it begins to impact leadership decisions, who can therefore be held accountable for failures to achieve them.

5.4. Processes and Decision-Making

Sustainability governance starts to influence corporate decision-making by encouraging the integration of environmental and social concerns into business strategy and long-term planning. While most firms are only beginning to make this transition, regulatory mandates and voluntary frameworks are compelling companies to look at how sustainability considerations intersect with financial performance and strategic risk. Issues such as climate change and labor practices, previously seen as secondary issues, are now being evaluated as relevant to business continuity and reputational resilience.

Frameworks such as the CSRD and ISSB currently request that businesses take into consideration how sustainability themes affect business models and financial results in the near term, middle term, and long term. The CSRD's dual materiality obligation, for example, requires companies to not only review how ESG drivers influence the company, but also consider how the company impacts society and the environment.[346] Such evaluations must be complemented with formalized management- and board-level procedures for dealing and monitoring material sustainability issues. Similarly, under California laws, companies are required to disclose the effect of climate-related risks and mitigation strategies, mandate that reflects a clear shift toward treating climate risk as a matter of corporate governance and strategic planning.

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[345] *See* EY, *Using ESG Dashboards and Metrics to Improve Risk Oversight* (Oct. 2022), https://www.ey.com/en_gl/climate-change-sustainability-services/esg-dashboards-and-metrics (last visited Aug. 9, 2025) (describing how dashboards and KRIs help organizations monitor ESG performance in real time).

[346] For more on CSRD's double materiality approach, *See* Matthias Täger, *'Double Materiality': What is It and Why Does It Matter?*, GRANTHAM RESEARCH INST. ON CLIMATE CHANGE & THE ENV'T (Apr. 21, 2021), https://www.lse.ac.uk/granthaminstitute/news/double-materiality-what-is-it-and-why-does-it-matter/; Francesco Mezzanotte, *Corporate Sustainability Reporting: Double Materiality Requires Rethinking Disclosure Practices*, J. CORP. ACCT. & FIN. (2023), https://www.tandfonline.com/doi/full/10.1080/14735970.2024.2319058.

Voluntary frameworks also support these obligations. The TCFD recommends disclosure of scenario analyses, governance structures, and climate-related metrics and targets, while the SBTi requires companies to set and pursue science-based emissions reduction targets. Together, these frameworks encourage firms to establish governance procedures that facilitate cross-functional cooperation and data-driven planning for climate resilience solutions.[347] These practices affect not just external reporting, but also internal processes such as capital allocation and R&D expenditure.[348] In essence, it shows that sustainability is no longer siloed; it is invited to be incorporated into strategy and risk-adjusted planning designs.

Additionally, as sustainability becomes more central to business strategy, numerous companies are establishing new governance frameworks to facilitate this shift. As noted earlier, some have created sustainability committees or cross-functional working groups involving legal, operations, and finance teams to ensure departmental alignment. Others have also implemented recurring scenario planning cycles to evaluate potential future risks, anything from regulatory innovation to climate-related disruptions and reputational threats.[349] To support integration more forcefully, key performance indicators (KPIs) are increasingly being linked to ESG commitments such as net-zero timelines, due diligence processes on suppliers, or DEI targets.[350]

These changes in processes are meant to enable boards and executives to monitor sustainability risks alongside financial risks and realign corporate strategies accordingly. They also impose internal accountability, as business units and leadership teams are now responsible for implementing sustainability-targeted initiatives and delivering measurable performance. When

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[347] *See* Amir Amel-Zadeh & George Serafeim, *Why and How Investors Use ESG Information: Evidence from a Global Survey*, 74 FIN. ANALYSTS J. 87, 88–90 (2018), http://dx.doi.org/10.2139/ssrn.2925310. (discussing the integration of ESG frameworks into corporate strategy and governance).

[348] *See* CAROLINA MACHADO & J. PAULO DAVIM, SUSTAINABLE MANAGEMENT FOR MANAGERS AND ENGINEERS 73–77 (2017) (explaining how voluntary sustainability frameworks drive governance integration and cross-functional collaboration).

[349] *See* SUSTAINALYTICS, *Setting SBTi Targets Is Good, But Far from Sufficient* (Feb. 21, 2025), https://www.sustainalytics.com/esg-research/resource/investors-esg-blog/setting-sbti-targets-is-good--but-far-from-sufficient (last visited Aug. 2, 2025) (noting companies are strengthening governance structures, linking board/executive pay to emissions-reduction KPIs, integrating carbon pricing, and engaging suppliers in GHG reduction targets).

[350] *Id.*

initiatives and metrics are disclosed, these changes also raise external accountability since they allow investors and other stakeholders to monitor performance.

5.5. Reconciliation with Traditional Corporate Governance

Despite the emergence of corporate sustainability governance, the transformations have largely occurred within the boundaries of existing corporate law. In the United States, especially under Delaware law, corporate directors continue to operate under the traditional framework of the business judgment rule, which affords wide discretion to boards, so long as decisions are made in good faith, with due care, and in the best interests of the corporation.[351]

This legal framework has proven flexible enough to accommodate the integration of environmental and social considerations into corporate governance, including board oversight, management risks process and control systems.[352] Indeed, corporate sustainability governance has expanded the range of factors boards and executives consider, but it has not altered the formal allocation of governance rights. Shareholders remain the only stakeholders with voting power, preserving traditional accountability structures and legal remedies of the conventional "corporate governance machine."[353] What has changed is how fiduciary duties are interpreted in light of the new added risks, especially when financially material, and how both regulatory and voluntary standards have raised expectations for how boards and management govern those risks.

Under the business judgment rule, directors are not precluded from considering all relevant factors, including climate or social issues, particularly where they are material to the long-term interests of the corporation and its shareholders.[354] In fact, most sustainability issues can fairly be

[351] *See, e.g.,* Adam Badawi, *The Business Judgment Rule*, in ENCYCLOPEDIA OF L. & ECON. 287 (2023) (comparing the wide discretion afforded to directors to negligence standards in force for other professionals, such as doctors).

[352] For more on the business judgment rule, *See, e.g.,* Lyman Johnson, *The Modest Business Judgment Rule*, 55 BUS. LAWYER 625, 631 (2000) (arguing that "[p]roperly understood, the business judgment rule is simply a policy of judicial non-review").

[353] *See* Dorothy S. Lund & Elizabeth Pollman, *The Corporate Governance Machine*, 121 COLUM. L. REV. 2563 (2021), https://scholarship.law.upenn.edu/faculty_scholarship/2775/.

[354] *Id.*

framed as long-term business issues. Even if their financial impact is not immediate or direct, they may ultimately influence a company's ability to attract and retain customers or employees, protect its reputation, maintain operational resilience against climate-related disruption, or avoid future legal liability for environmental or human rights damage in its operations or supply chains. As such, directors have a sound legal basis to include sustainability considerations in their decision-making without breaching fiduciary duties.

Boards of directors remain protected under the business judgment rule as long as they engage in informed decision-making regarding sustainability risks, whether it is complying with legislation or responding to investor requests for sustainability reporting. Moreover, by establishing robust sustainability governance structures, due diligence procedures, and executive accountability for sustainability, whether beneath obligatory regulations or voluntary initiatives, corporate leaders can further strengthen their demonstration of prudence. Such governance actions are evidence that the board acted responsibly in pursuing and managing material risks, further grounding their protection under traditional fiduciary principles.

Thus, boards may (and indeed must) consider stakeholder impacts, sustainability goals, or reputational hazards as part of their risk management and strategy oversight, not because stakeholder interests are superior to shareholder ones, but because the definition of prudent management has evolved.[355] This legal wiggle room is key to explaining how U.S. companies have adopted ESG governance practices without legislative changes to corporate purpose statutes. Norms of governance for sustainability are shifting not in opposition to corporate law, but via corporate law.

Apart from that, it is important to state that corporate sustainability governance complements, instead of weakening, traditional oversight structures. Accountability through transparency is a primary characteristic: disclosure requirements, whether regulatory or voluntarily assumed, enable investors and stakeholders to closely scrutinize board-level decisions, review

[355] *See* Martin Lipton, Sabastian V. Niles & Marshall L. Miller, *Risk Management and the Board of Directors*, HARV. L. SCH. F. ON CORP. GOVERNANCE (Mar. 20, 2018), https://corpgov.law.harvard.edu/2018/03/20/risk-management-and-the-board-of-directors-5/ (last visited Jan. 12, 2025) (highlighting that boards' oversight duties—rooted in fiduciary care—extend to evolving corporate strategies and risk frameworks, which now encompass sustainability concerns).

trade-offs, and determine if environmental and societal risks are being properly addressed. Public disclosure on sustainability plans, goals, and performance invites external scrutiny and pressure, thus highlighting internal accountability arrangements.

Importantly, control remains firmly in the hands of corporate boards. Climate and sustainability frameworks don't supplant board control but rather broaden the scope of issues boards should oversee. These risks, once considered peripheral, are now treated with the same seriousness as financial ones. The integration is such that sustainability finds its way into essential governance practices such as board committee deliberations, strategic planning, and risk management.

In addition, sustainability governance can enhance managerial discipline. It introduces formalized requirements such as third-party assurance of disclosures, scenario analysis for climate-related risks, and periodic measurement of performance against stated targets. These mechanisms reduce the space for managerial discretion, discourage greenwashing, and encourage alignment between stated sustainability goals and operational behavior.

Taken together, these features resonate with the hybrid nature of corporate sustainability governance: it is shaped by a mix of regulatory requirements, voluntary norms, and market pressures. And while its content continues to evolve, it does so within the conventional corporate governance framework, reinforcing the dominance of fiduciary duties, institutional checks, and strategic accountability.

5.6. Effectiveness Remains an Open Question

As demonstrated in earlier sections, corporate sustainability governance is reshaping internal organization's structures, but its success in terms of producing material environmental or societal outcomes is a long way from guaranteed. Much of regulatory and voluntary initiatives rely on transparency and disclosure to drive behavioral alteration, but an open question exists as to whether these mechanisms will be translated into real adjustments in business habits.[356] As

[356] *See, e.g.,* Steven Davidoff Solomon and Claire Hill, *Limits of Disclosure*, 36 Seattle U. L. REV. 599 (2013), available at https://scholarship.law.umn.edu/faculty_articles/181 (debating the limits of disclosure and arguing that

governance scholarship evolves, it must assess not only how sustainability is institutionalized, but also whether it achieves its intended impact.

Despite these challenges, there are strong reasons to believe that corporate sustainability governance, once internalized, will not easily disappear. Sustainability disclosure and governance practices are now ubiquitous for large public companies, and even in the face of backlash or political narrative shift, the governance architecture around it will probably remain. Companies continue to maintain board committees, cross-functional sustainability working groups, and executive positions tied to sustainability. These governance features now reside in compliance, enterprise risk, and strategic planning, not just because of regulation, but because they also support meeting investor needs, reputational requirements, and market positioning.

Once these mechanisms are institutionalized and routinized, they tend to create institutional inertia.[357] Pulling them down would not only be costly, but possibly expose companies to legal and reputational risks, particularly where companies have made public sustainability commitments.[358] In that sense, while the legal argument over ESG might shift, the underlying change in governance that it has introduced is likely to persist. Even as the language changes or the momentum in policy declines, sustainability governance is now ingrained in the culture of modern corporate governance.[359]

On that premise, then, the future of ESG may not really rest on the term itself but on the governance system that it has facilitated.[360] The branding may vary, and the policy trajectory may change from one moment to the next, but the internal mechanisms, oversight arrangements, and accountability machinery ushered in under the sustainability umbrella are now part of the default operating system for modern corporate governance.

"disclosure is too often a convenient path for policymakers and many others looking to take action and hold onto comforting beliefs in the face of a bad outcome.").

[357] *See* Fairfax, *supra* note 280, at 1037-1050.

[358] *Id.*

[359] *See* Alex Edmans, *The End of ESG*, 52 FIN. MGMT. 3 (2023), http://dx.doi.org/10.2139/ssrn.4221990 (arguing that ESG is both "extremely important" and "nothing special," and should be integrated into mainstream investing rather than treated as a niche).

[360] *Id.*

6. Conclusion

This article presented the emergence of corporate sustainability governance, which represents a quiet, yet far-reaching transformation in how firms govern themselves. While rooted in existing legal frameworks and fiduciary principles, it has introduced new structures and processes, expanding the reach of governance to encompass environmental and social risks, long-term strategic planning, and cross-functional accountability.

This shift has been driven not by a single source, but by the convergence of regulatory requirements and voluntary initiatives, reinforced by investor demands, evolving market expectations, and broader societal concerns. It encompasses not only climate issues but also social matters, as reflected in frameworks such as the CSDDD and the ISSB standards, as well as in voluntary initiatives. In sum, regulations such as the EU's CSRD and CSDDD, the ISSB standards, and California's climate disclosure laws have prompted companies to formalize their sustainability governance arrangements. At the same time, firms' voluntary commitments to sustainability goals and reporting initiatives, along with integration of sustainability performance into executive compensation, have further advanced these changes.

Importantly, this transformation has not required rewriting corporate law. Existing principles, particularly the business judgment rule and the central role of boards, have accommodated sustainability governance. Directors continue to enjoy great freedom to take sustainability factors into account so long as they are consistent with the long-term interests of the firm. Rather than replacing traditional governance, sustainability practices have extended it, incorporating new rituals of oversight and a broader definition of risk. And these practices have become institutionalized, which means that they will not be so readily dismantled, even during a period of political backlash and rhetorical turbulence. Whether we call it ESG, sustainability or something else, the governance systems it has built are now part of the architecture of modern corporate oversight.

Part III

Can ESG Culture Be Acquired? The Impact of M&A on Sustainability Practices and Market Perceptions

1. Introduction

In recent years, corporations have been under great pressure to redefine their purpose[818] and develop a corporate culture that encompasses the interests of society, rather than just those of shareholders.[819] The escalating threats of climate change[820] and global economic inequality,[821] compounded by governments' slow pace to regulate corporate externalities and address social challenges,[822] have created the momentum for the growth of the environmental, social and governance (ESG) agenda.[823] This push for businesses to integrate ESG considerations into their

[818] *See generally* Edward B. Rock, *For Whom Is the Corporation Managed in 2020? The Debate Over Corporate Purpose,* 76 BUS. LAW. 363 (2021); Lucian A. Bebchuk & Roberto Tallarita, *The Illusory Promise of Stakeholder Governance,* 106 CORNELL L. REV. 91 (2020).

[819] For an overview of the shareholder primacy theory, which has been the dominant view of corporate law for decades, *See, e.g.,* Michael C. Jensen & William H. Meckling, *Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure*, 3 J. FIN. ECON. 305, 305 (1976); William W. Bratton & Michael L. Wachter, *Shareholder Primacy's Corporatist Origins: Adolf Berle and The Modern Corporation*, 34 J. CORP. L. 99, 120 (2008); Henry Hansmann & Reinier Kraakman, *The End of History for Corporate Law*, 89 GEO. L.J. 439, 440-42 (2001). For a corporate law view of stakeholder governance, *See, e.g.,* Margaret M. Blair & Lynn A. Stout, *A Team Production Theory of Corporate Law*, 85 VA. L. REV. 247, 308-09 (1999).

[820] *See* NICHOLAS STERN, THE ECONOMICS OF CLIMATE CHANGE: THE STERN REVIEW (2007) (providing an economic analysis of climate change and the financial consequences of inaction); JOHN HOUGHTON, GLOBAL WARMING: THE COMPLETE BRIEFING (Cambridge Univ. Press 2004) (discussing the scientific basis for global warming and its potential global and societal impacts).

[821] *See* THOMAS PIKETTY, CAPITAL IN THE TWENTY-FIRST CENTURY (Harvard Univ. Press 2014) (analyzing the rising global economic inequality and the historical trends behind it); FRANÇOIS BOURGUIGNON, THE GLOBALIZATION OF INEQUALITY (Princeton Univ. Press 2016) (examining the impact of globalization on income inequality, particularly in developing nations).

[822] See, e.g., JOSEPH E. STIGLITZ, MARKET FAILURE AND THE ECONOMIC ROLE OF GOVERNMENT (1989) (discussing the role of government in addressing market failures, including the regulation of corporate externalities).

[823] *See, e.g.,* Dorothy S. Lund, *Toward a Dynamic View of Corporate Purpose*, EUR. CORP. GOVERNANCE INST. – LAW WORKING PAPER NO. 746/2023 (Dec. 14, 2023), https://ssrn.com/abstract=4665040 (suggesting that

strategies and decision-making has been further accelerated by a combination of investor activism,[824] consumer preferences favoring companies with strong ESG commitments,[825] and expanding regulatory mandates.[826]

Despite recent backlash in the United States,[827] where ESG has become a highly politically charged issue,[828] debates over the role of sustainability in corporate governance and investment decisions remain highly relevant.[829] While the pushback is likely to impact ESG evolution, leading to corporate retrenchment—such as scaling back commitments,[830] exercising greater caution in

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the welfare-maximizing purpose for corporations could change depending on external economic conditions and analyzing two historical periods in which the dominant view of corporate purpose in society changed dramatically).

[824] *See, e.g.,* Subodh Mishra, *U.S. Shareholder Proposals: A Decade in Motion*, HARV. L. SCH. F. ON CORP. GOVERNANCE (Nov. 18, 2024), https://corpgov.law.harvard.edu (last visited Jan. 3, 2025) (exploring how ESG topics outnumbered governance and compensation requests in shareholder proposals in the US over the past four years, with climate change and human capital management driving the surge).

[825] *See, e.g.,* Michal Barzuza, Quinn Curtis & David H. Webber, *The Millennial Corporation: Strong Stakeholders, Weak Managers*, 28 STAN. J.L. BUS. & FIN. 255 (2023) (arguing that increasing demand for socially responsible corporate behavior, originating in but not limited to the millennial generation, has created powerful incentives for corporate managers to promote ESG goals).

[826] *See, e.g.,* Archie Burkinshaw, *ESG Regulation in 2024: Everything You Need to Know*, SUSTAINABILITY NEWS (Jan. 2, 2024), https://sustainability-news.net/policy-and-regulation/2024-guide-to-esg-regulation/ (last visited Apr. 3, 2025).

[827] *See, e.g.,* Charles Donefer, *State ESG Laws in 2023: The Landscape Fractures*, THOMSON REUTERS (May 31, 2023), https://www.thomsonreuters.com/en-us/posts/esg/state-laws/ (last visited Feb. 8, 2025) (explaining that several U.S. states have enacted laws to limit the consideration of ESG factors in public investments); Julie Bykowicz & Angel Au-Yeung, *Conservatives Have a New Rallying Cry: Down with ESG*, WALL ST. J. (Feb. 26, 2023, 5:30 AM ET), https://www.wsj.com/articles/conservatives-have-a-new-rallying-cry-down-with-esg-2ef98725 (last visited Feb. 8, 2025); Lyle Moran, *Climate Lawsuits Against Largest Fossil Fuel Producers Have Almost Tripled*, ESG DIVE (Sep. 25, 2024), https://www.esgdive.com/news/climate-lawsuits-against-largest-fossil-fuel-producers-have-almost-tripled/728069/ (last visited Feb. 8, 2025) (showing that lawsuits have emerged against companies for allegedly prioritizing ESG to the detriment of profits or for misleading stakeholders through greenwashing).

[828] *Id.*

[829] *See, e.g.,* Sarah C Haan, *Shareholder Proposal Settlements and the Private Ordering of Public Elections*, 126 YALE L. J. 262 (2016) (showing that shareholder proposals regularly demand transparency on company ESG plans and impacts).

[830] *See, e.g.,* Kenneth P. Pucker, *Companies Are Scaling Back Sustainability Pledges. Here's What They Should Do Instead*, HARV. BUS. REV. (Aug. 20, 2024), https://hbr.org/2024/08/companies-are-scaling-back-sustainability-pledges-heres-what-they-should-do-instead (last visited Mar. 15, 2025); Nathaniel Bullard, *Big Oil's Pullback From Clean Energy Matters Less Than You Might Think*, BLOOMBERG (June 25, 2023), https://www.bloomberg.com/news/articles/2023-06-25/big-oil-s-pullback-from-cleanenergy-matters-less-than-you-d-think?embedded-checkout=true; Evan Halper, *BP Dials Back Climate Pledge Amid Soaring Profits*, WASH. POST (Feb. 7, 2023), https://www.washingtonpost.com/business/2023/02/07/bp-climateemissions-oil-profits/.

disclosure,[831] and rebranding ESG-related departments and initiatives[832] —, global ESG regulations remain in place and are likely to spread worldwide.[833] Moreover, many companies have already integrated ESG into their governance structures and operational processes, making a full retreat from ESG both impractical and unlikely.[834] Additionally, the publication of voluntary ESG reports continues to rise,[835] and investments in sustainable assets have remained strong, accounting for more than a quarter of global financial assets under management, totaling approximately $30 trillion.[836]

As ESG has taken center stage in the business community, it has also become a major focus in academic literature. Scholars in corporate law and economics have developed an extensive body of research on how ESG culture, a reflection of a firm's environmental and social practices, influences a variety of business outcomes. One area of inquiry considers the role of ESG in mergers and acquisitions (M&A), which are often major events that transform firms' operations and strategic direction. In this context, studies have primarily examined how ESG factors influence M&A outcomes such as deal success, bid announcements, and investor responses.[837] However,

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[831] *See* Lisa M. Fairfax, *ESG's Death Defying Future: Predicting the Future of ESG Through the Lens of Current ESG Disclosure*, 26 U. PA. J. BUS. L. 1019, 1041 (2024), https://scholarship.law.upenn.edu/cgi/viewcontent.cgi?article=1717&context=jbl (discussing the possible impact of ESG pushback on disclosure and finding that reduced disclosure *See*ms highly unlikely for several reasons).

[832] *See, e.g.,* Tim Mohin, *Another ESG Rebrand?*, ESG & CLIMATE NEWS (Mar. 7, 2025), https://www.esgandclimatenews.com/p/another-esg-rebrand (last visited Mar. 15, 2025); Isla Binnie, *BlackRock's Fink Says He's Stopped Using 'Weaponized' Term ESG*, REUTERS (June 26, 2023), https://www.reuters.com/business/environment/blackrocks-fink-says-hes-stopped-using-weaponised-term-esg-2023-06-26/ (last visited Mar. 15, 2025).

[833] Although the European Union has proposed some changes to its ESG directives, most of their content is preserved. *See* EUR. COMM'N, *Commission Proposes to Cut Red Tape and Simplify Business Environment* (Feb. 26, 2025), https://commission.europa.eu/news/commission-proposes-cut-red-tape-and-simplify-business-environment-2025-02-26_en.; Lamar Johnson, *EU Adopts Omnibus Proposal, Trims Sustainability Reporting Requirements*, ESG DIVE (Feb. 27, 2025), https://www.esgdive.com/news/eu-omnibus-trims-csrd-csddd-reporting-requirements-timelines/741161/ (last visited Mar. 3, 2025.

[834] *See, e.g.,* Fairfax, *supra* note 14 (arguing that the universality and pervasiveness of ESG reflected in the existing disclosure landscape makes talks of ESG's demise unrealistic and implausible).

[835] *See* G&A INSTITUTE, *2023 Sustainability Reporting in Focus (2023)*, https://www.ga-institute.com/research/research/sustainability-reporting-trends/2023-sustainability-reporting-in-focus/ (last visited Mar. 3, 2025).

[836] *See* GLOBAL SUSTAINABLE INV. ALL, *Global Sustainable Investment Review 2022*, GSIA (2022), https://www.gsi-alliance.org/members-resources/gsir2022/ (last visited Mar. 15, 2025).

[837] *See, e.g.,* Nihat Aktas, Eric De Bodt & Jean-Gabriel Cousin, *Do Financial Markets Care about SRI? Evidence from Mergers and Acquisitions*, 35 J. BANKING & FIN. 1753 (2011),

significantly less attention has been given to the reverse relationship: how M&A transactions affect ESG performance.[838] Only a handful of studies have explored the extent to which M&A transactions can drive changes in the ESG culture of the acquirer.[839]

While the process of establishing corporate culture is long and ongoing, abrupt changes, such as shifts in leadership, financial crises, or strategic transactions, can disrupt or reinforce these commitments.[840] Among such events, M&A has the potential to represent a particularly complex and consequential disruption to ESG culture.[841] When two firms merge, they bring together different corporate cultures, governance structures, and stakeholder expectations, creating both opportunities and challenges for ESG no post-deal. While some acquirers may actively seek to enhance their ESG culture by acquiring firms with strong sustainability credentials, others may deprioritize ESG in favor of financial or operational efficiencies. Moreover, the post-merger integration process determines whether ESG commitments are strengthened, diluted, or fundamentally transformed.[842]

This gap in the literature on how M&A impacts ESG culture raises important questions: Do acquiring firms improve or weaken their ESG culture after an M&A transaction? Does the ESG performance of the target firm influence the acquirer's post-merger sustainability trajectory? And how do factors such as industry characteristics and company size moderate these outcomes? This paper examines whether M&A operations serve as a catalyst for changes in ESG culture.

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https://doi.org/10.1016/j.jbankfin.2010.11.006; Mathieu Gomes & Sylvain Marsat, *Does CSR Impact Premiums in M&A Transactions?*, 26 FIN. RES. LETTERS 71 (2018), https://doi.org/10.1016/j.frl.2017.12.005.

[838] *See* Stuart L. Gillan, Andrew Koch & Laura T. Starks, *Firms and Social Responsibility: A Review of ESG and CSR Research in Corporate Finance*, 66 J. CORP. FIN. 101889 (2021), https://doi.org/10.1016/j.jcorpfin.2021.101889.

[839] *See* Ioannis Tampakoudis & Evgenia Anagnostopoulou, *The Effect of Mergers and Acquisitions on Environmental, Social and Governance Performance and Market Value: Evidence from EU Acquirers*, 29 BUS. STRATEGY & ENV'T 1865 (2020), https://doi.org/10.1002/bse.2475.

[840] *See* Silvia Fregoni, *Beyond Tone at the Top: A Taxonomy of What Drives Corporate Culture Change* (unpublished manuscript) (on file with author) (Part I of this dissertation).

[841] *Id.* at 55.

[842] *See* Melissa E. Graebner, Koen H. Heimeriks, Quy Nguyen Huy & Eero Vaara, *The Process of Post-Merger Integration: A Review and Agenda for Future Research*, U. OXFORD RSCH. ARCHIVE (2020), https://ora.ox.ac.uk/objects/uuid%3Aeab00102-5fc7-4bc2-9ae4-9fd30bdee804/files/rx633f114m (reviewing three decades of scholarship on post-merger integration and arguing that integration processes, particularly strategic, sociocultural, and learning dimensions, are central to M&A success).

Specifically, it investigates whether acquiring a target with a higher ESG culture enhances the acquirer's ESG performance, and conversely, whether acquiring a target with lower ESG commitments weakens the acquirer's ESG culture.

For this study, I use ESG performance, measured through the ESG scores provided by FactSet Truvalue,[843] as a proxy for ESG culture and sustainability practices. The dataset initially comprised 894 M&A transactions between publicly traded companies from 2007 to 2018, in which at least one party was U.S.-based and ESG scores were available for both the acquirer and the target. From this initial pool, I derived a final sample of 250 deals by retaining only those with ESG scores consistently available across all analyzed timeframes. Using a dataset of M&A deals across multiple industries and jurisdictions, I assess whether firms experience a post-merger improvement or decline in ESG performance and examine the factors that may influence this variation.

Additionally, this paper investigates whether ESG acts as a driver of value creation. It examines the financial implications of M&A deals between firms with differing ESG cultures. Specifically, it investigates the impact of acquiring a target with a higher ESG culture on the acquirer's stocks' cumulative abnormal returns (CARs). It also examines a second scenario: whether acquiring a target with lower ESG culture negatively affects the acquirer's abnormal returns. If ESG is indeed value-increasing, as claimed by many stakeholder supporters,[844] then firms acquiring targets with superior ESG cultures tend to see improvements in their corporate value.

This study presents two core findings. First, M&A transactions can act as catalysts for ESG culture change in acquiring firms. Acquirers that purchase targets with stronger ESG profiles are associated with significant and sustained improvements in their own ESG culture post-merger. This result supports the culture synergy theory, which predicts that acquirers can learn from targets' best practices, acquiring knowledge that helps them overcome prior shortcomings or organizational inertia in order to improve ESG culture. The improvement is most pronounced

[843] *See* FACTSET, *FactSet Truvalue Scores & Spotlights*, https://www.factset.com/marketplace/catalog/product/factset-truvalue-scores-and-spotlights (last visited Apr. 3, 2025).

[844] *See, e.g.,* Blair & Stout, *supra* note 2.

when the acquirer is moderately or much larger than the target, suggesting that scale may facilitate the adoption of ESG practices. Conversely, acquiring a lower-ESG target is associated with declining ESG performance, although not always statistically significant.

Second, while ESG-enhancing acquisitions improve ESG culture, they do not produce statistically significant abnormal stock returns in the short or medium term. Although market reactions are directionally positive, supporting the view that ESG may create long-term value, investors appear cautious, possibly due to concerns around integration risks or delayed ESG-related synergies. Relative size between acquirers and targets seems, indeed, seems more significant to the abnormal returns. Acquirers that are significantly larger than their targets tend to achieve stronger returns, independent of ESG scenario, indicating that scale, rather than ESG culture, is a more consistent driver of financial performance in M&A transactions up to one year after the deal.

These findings contribute to the growing literature on the drivers of corporate culture change, M&A strategy, and the broader significance of ESG in corporate decision-making. They offer practical insights for managers and investors seeking to understand how ESG considerations affect post-merger outcomes and may inform strategic planning around acquisitions. For policymakers, the results underscore the potential relevance of ESG data in capital markets, supporting ongoing efforts to evaluate and improve ESG disclosure frameworks. This paper departs from earlier work by examining longer post-merger time horizons and by analyzing deals involving both higher- and lower-ESG targets.

The article is organized as follows. Part 2 lays out the background and the literature review for this analysis. Part 3 develops the theoretical framework and the testable hypotheses, and Part 4 explains the data sources and the methodology of this investigation. Part 5 presents the results, and Part 6 discusses implications. Part 7 concludes.

2. Background and Literature Review

2.1. The Growing Importance of Corporate Culture

Corporate culture has emerged as a central issue in contemporary debates about the role of corporations in society.[845] As the ideological divide between shareholder primacy and stakeholder capitalism intensifies, corporate culture arises as the underlying framework that aligns individuals and systems to the corporation's chosen purpose. Regardless of whether a company prioritizes shareholder returns, stakeholder interests, or some mix of the two, its culture comprises the values, norms, and practices that dictate how these objectives are being pursued.[846]

In recent years, corporate culture has become increasingly recognized as a significant factor impacting business strategy, with possible implications for risk management and value creation.[847] Both scholars and practitioners seem to agree that a healthy corporate culture improves organizational cohesion,[848] increases employee commitments,[849] and contributes to business success.[850] On the opposite side, a dysfunctional or toxic culture can lead to corporate scandals,[851]

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[845] For recent discussions on corporate purpose, *See generally* Jill E. Fisch & Steven Davidoff Solomon, *Should Corporations Have a Purpose?*, 99 TEX. L. REV. 1309 (2021). *See also* Rock, *supra* note 1.

[846] *See, e.g.,* EDGAR H. SCHEIN, ORGANIZATIONAL CULTURE AND LEADERSHIP 17 (Jossey-Bass 5th ed. 2017), for a well-accepted definition of corporate culture (defining corporate culture as "a pattern of shared basic assumptions learned by a group as it solved its problems of external adaptation and internal integration, which has worked well enough to be considered valid and, therefore, to be taught to new members as the correct way to perceive, think, feel, and behave in relation to those problems").

[847] *See, e.g.,* John R. Graham, Jillian Grennan, Campbell R. Harvey & Shivaram Rajgopal, *Corporate Culture: Evidence from the Field*, 146 J. FIN. ECON. 552 (2022) (reporting that 92% of surveyed executives believe improving corporate culture would increase firm value, and linking culture to ethical choices, innovation, and value creation).

[848] *See* Joseph T. Mahoney, *Chester Barnard's Management Theory: Overview*, STUDY.COM, https://study.com/academy/lesson/chester-barnards-management-theory-lesson-quiz.html (last visited Mar. 15, 2025) (reviewing Barnard's management theory, highlighting his perspective on organizations as cooperative systems and the importance of both formal and informal structures in achieving organizational cohesion).

[849] *See, e.g.,* Cătălina Radu, *Fostering a Positive Workplace Culture: Impacts on Performance and Agility*, in HUM. RES. MGMT.—AN UPDATE (IntechOpen 2023), https://doi.org/10.5772/intechopen.1003259.

[850] *See, e.g.,* ERIC G. FLAMHOLTZ & YVONNE RANDLE, CORPORATE CULTURE: THE ULTIMATE STRATEGIC ASSET (Stanford Univ. Press 2011).

[851] *See, e.g.,* Donald C. Langevoort, *The Behavioral Economics of Corporate Fraud*, 65 STAN. L. REV. 1297 (2013).

regulatory violations,[852] and reputational damage,[853] harming both financial performance and public trust.[854]

Corporate culture has been studied in a variety of fields. Psychologists examine it in the context of individual and group behavior, trying to understand the role of social interaction and leadership in workplace norms.[855] Sociologists study corporate culture as a social structure with a focus on the institutionalization of power, values and how organizations establish and maintain identities.[856] Economists, for their part, usually consider corporate culture as an intangible asset that are difficult to measures but can help companies to increase public confidence and align employees' expectations, for example.[857] Legal scholars often discuss how corporate culture impacts compliance, governance, and corporate liability, particularly in corporate misconduct, fiduciary duty, and regulatory enforcement.[858] This fragmentation has resulted in a myriad of definitions and approaches to corporate culture study, and, as such, an interdisciplinary discussion is needed to determine a more informed understanding of its role.

While there is no universal definition, there is a great understanding that corporate culture is formed by shared assumptions, values, and beliefs that govern general behavior in an organization. Edgar Schein, one of the most influential theorists in this field, defines corporate culture as a collection of "artifacts, espoused values, and basic underlying assumptions" that

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[852] *See, e.g.,* JOHN M. CONLEY, ENRON: *The Collapse of Corporate Culture*, in PERSPECTIVES IN BUSS. ETHICS 233 (Laura P. Hartman ed., Mcgraw-Hill 3d ed. 2005).

[853] *See, e.g.,* EUGENE SOLTES, WHY THEY DO IT: INSIDE THE MIND OF THE WHITE-COLLAR CRIMINAL 56 (PublicAffairs 2016).

[854] *See, e.g.,* Mihailis E. Diamantis, *Corporate Criminal Minds*, 91 NOTRE DAME L. REV. 2049 (2016).

[855] *See, e.g.,* Kurt Lewin, *Frontiers in Group Dynamics*, 1 HUM. REL. 5 (1947) (setting the groundwork for subsequent research into how group behaviors and social interactions shape organizational norms and culture).

[856] *See, e.g.,* ROBERT JACKALL, MORAL MAZES: THE WORLD OF CORPORATE MANAGERS (Oxford Univ. Press 1988) (providing a critical sociological perspective on corporate culture, exploring how bureaucratic environments shape the moral consciousness and actions of managers).

[857] *See, e.g.,* PAUL MILGROM & JOHN ROBERTS, ECONOMICS, ORGANIZATION, AND MANAGEMENT (Prentice Hall 1992) (analyzing how corporate culture, viewed as an intangible asset, can enhance efficiency by reducing transaction costs, fostering trust, and aligning employee expectations).

[858] *See, e.g.,* Luigi Guiso, Paola Sapienza & Luigi Zingales, *The Value of Corporate Culture*, 117 J. FIN. ECON. 60 (2015) (examining how corporate culture influences firm performance, compliance, and governance, and finding that companies with strong ethical cultures experience fewer instances of corporate misconduct and regulatory violations).

impact decision-making and workers relations.[859] His model highlights the differences between the observable manifestations of culture, such as office design, dress code and company slogans, explicit principles often written in codes of ethics or conduct, and underlying and unstated assumptions that dictate action.[860] From an economic perspective, David Kreps and Cremer believe that corporate culture is a way to ensure employees' coordination and help firms navigate uncertainties.[861] When "unforeseen contingencies arise,"[862] parties may need to trust each other to decide the right thing to do.[863] This view shows corporate culture as an implicit governance system that mitigates agency problems between managers and investors and contributes to companies' resilience.[864] Similarly, scholars in management and organizational studies, such as Charles O'Reilly, highlight the significance of corporate culture in creating cohesion and aligning employees with corporate objectives.[865]

Therefore, it is safe to conclude that corporate culture plays numerous roles in organizations. First, it grants employees identity and a sense of belonging, reinforcing commitment to corporate goals and improving job satisfaction.[866] Second, research indicates that organizations with strong, well-defined cultures have fewer turnovers, are more productive, and manage better

[859] *See* Schein, *supra* note 29.

[860] *Id.*

[861] *See* DAVID M. KREPS, *Corporate Culture and Economic Theory*, in PERSPECTIVES ON POSITIVE POLITICAL ECONOMY 90 (James E. Alt & Kenneth A. Shepsle eds., CAMBRIDGE UNIVERSITY PRESS 1990).

[862] *See* Jacques Crémer, *Corporate Culture and Shared Knowledge*, 6 INDUS. & CORP. CHANGE 351 (1997), https://doi.org/10.1093/icc/6.3.351 (last visited Aug. 6, 2025).

[863] *See* Benjamin E. Hermalin, *Economics & Corporate Culture*, 15 J. ECON. PERSP. 3, 3-13 (2000) (explaining Kreps's model of corporate culture).

[864] *See* Kreps, *supra* note 44.

[865] *See, e.g.,* Charles A. O'Reilly III & Jennifer A. Chatman, *Corporations, Culture, and Commitment: Motivation and Social Control in Organizations*, 18 CAL. MGMT. REV. 9 (1996), https://www.researchgate.net/publication/303455136_Corporations_Culture_and_Commitment_Motivation_and_Social_Control_in_Organizations (arguing that culture is important for both the implementation of strategy and as a mechanism for generating commitment among organizational members).

[866] *See, e.g.,* Eric W. MacIntosh & Alison Doherty, *The Influence of Organizational Culture on Job Satisfaction and Intention to Leave*, 13 SPORT MGMT. REV. 106 (2010) (demonstrating that a positive organizational culture enhances job satisfaction and reduces turnover intentions).

industry or economic changes.[867] Culture is also an unofficial system of control that can shape behavior in ways that policy and formal regulation cannot. By organizing workplace expectations and norms, corporate culture eliminates the need for excessive monitoring and hierarchical control and improves responsibility among employees.[868] And corporate culture also influences company's risk tolerance, which defines the way a firm responds to crises and regulatory pressure.[869]

Corporate culture is typically confused with related but distinct organizational concepts, so it is necessary to make its conceptual boundaries clear. Corporate culture is not a company's formal mission statement or other stated purpose document, that often articulates aspirational values, not daily realities.[870] Mission statements can influence culture but do not, in themselves, define it.[871] Instead, culture is created through daily behavior, unwritten rules, and the collective experiences of employees. Similarly, corporate culture is distinct from corporate strategy, which establishes a company's competitive posture and business objectives.[872] While strategy defines a roadmap for a company to achieve its goals, culture determines how leadership and employees implement it, or even how the goals are initially defined.[873] A solid strategy can fail if the existing corporate culture does not facilitate its execution.[874] Furthermore, corporate culture is different from corporate governance, which refers to the official structures and mechanisms that control decision-making.[875]

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[867] *See, e.g.,* JOHN P. KOTTER **&** JAMES L. HESKETT**,** CORPORATE CULTURE AND PERFORMANCE 11–12 (Free Press 1992) (finding that firms with strong, adaptive cultures have lower turnover, higher productivity, and greater capacity to adapt to industry and economic change).

[868] *See* Michael Roos, Jessica Reale & Frederik Banning, *The Effects of Incentives, Social Norms, and Employees' Values on Work Performance* [econ.TH] (last revised July 22, 2021) (working paper), arXiv:2107.01139 .(examining how organizational culture influences self-regulation and accountability among employees).

[869] *See* GEERT HOFSTEDE, GERT JAN HOFSTEDE & MICHAEL MINKOV, CULTURES AND ORGANIZATIONS: SOFTWARE OF THE MIND 344–46 (McGraw-Hill 3d ed. 2010) (discussing how organizational culture shapes risk tolerance and responses to external pressures).

[870] *See, e.g.,* JILLIAN GRENNAN & KAI LI, *Corporate Culture: A Review and Directions for Future Research*, in HANDBOOK OF FIN. DECISION MAKING 112, 113 (Gilles Hilary & David McLean eds., 2023)

[871] *Id.*

[872] *See* Jan Van den Steen, *Culture as a Driver of Strategy*, 9 AM. ECON. J. 1, 1 (2017).

[873] *See generally* Robert Gibbons, John Siegel & Richard A. Weber, *Strategy Meets Culture (for Breakfast): Understanding the Relationship and Highlighting its Potential*, 6 STRATEGY SCI. 111 (2021).

[874] *See* Sotirios Paroutis & Loizos Heracleous, *Culture vs Strategy: Which to Precede, Which to Align?*, RESEARCHGATE (2013).

[875] *Id.*

Governance arrangements influence culture as they set expectations for leadership behavior and compliance,[876] but it is not enough to define culture, which depends also on ongoing interactions from companies' employees.

Another common mistake is confusing corporate culture with regulatory compliance. Compliance means adherence to laws, regulations, and industry standards, while corporate culture consists of internal norms and values that shape decision-making beyond legal compliance.[877] A company may have a great compliance program but a poor ethical culture, leading to a "check-the-box" approach to regulation rather than true corporate responsibility.[878] On the other hand, corporations with good ethical cultures are more likely to include compliance in their corporate values, thus promoting an affirmative approach to risk management and governance.[879]

Although corporate culture is often considered deeply rooted in organizations, it is not immutable. Scholars have observed that culture can evolve over time in response to internal and external pressures.[880] However, there is considerable debate over how easily and how often culture actually change: many argue it tends to be a slow and complex process,[881] with some suggesting that culture is inherently resistant to change.[882] Leadership succession,[883] marketplace

[876] *See generally* Adam B. Badawi & Robert Bartlett, *ESG Overperformance? Assessing the Use of ESG Targets in Executive Compensation Plans*, STAN. L. & ECON. OLIN WORKING PAPER NO. 592, (Aug. 29, 2024), available at https://ssrn.com/abstract=4941016.

[877] *See, e.g.,* Stavros Gadinis & Amelia Miazad, *The Hidden Power of Compliance*, 103 MINN. L. REV. 1393, 1397 (2018), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3123987.

[878] *Id. See also* Dennis Campbell & Tatiana Sandino, *Corporate Governance, Compliance, and Culture: The Role of Integrity in Driving Performance*, 56 J. ACCT. RES. 1, 3 (2018).

[879] *Id.*

[880] *See, e.g.,* Grennan & Li, *supra* note 53 (arguing that corporate culture is reinforced by individuals (e.g., leaders), systems (e.g., executive compensation), and events (e.g., mergers)).

[881] *See, e.g.,* Gary B. Gorton & Alexander K. Zentefis, *Corporate Culture as a Theory of the Firm*, NBER WORKING PAPER No. 27353, at 44-45 (June 2020), https://www.nber.org/papers/w27353.

[882] *See, e.g.,* JOHN P. KOTTER, LEADING CHANGE 125 (Harvard Bus. Review Press 1996) (emphasizing that changing corporate culture is one of the most difficult challenges an organization faces).

[883] *Id.* (emphasizing that creating a sense of urgency and aligning organizational resources through committed leadership are essential for driving successful cultural change initiatives). *See also* Schein, *supra* note 29.

conditions,[884] regulatory shifts,[885] and societal norms all play a role in shaping corporate culture over time. Importantly, it is much easier to change written aspects of the culture, such as policies and codes, than values engrained in the firm, which can create a disconnect between what a company says and what it actually practices.[886]

Therefore, the adaptability of corporate culture can allow organizations to be flexible and more competitive, but can also create challenges if not aligned with strategic objectives.[887] In such cases, it may lead to internal conflict and limit the effectiveness of change efforts, or invite external scrutiny when public messaging diverges from actual practices. For example, companies that openly advocate innovation but have bureaucratic, rigid cultures shall be unable to create revolutionary change, and companies that advocate ethical leadership but tolerate toxic workplace cultures compromise their credibility.[888]

Although much has been written on the general theory of corporate culture, there remains a significant gap in research on the specific drivers of culture change and how it happens in practice. This study aims to contribute to filling this gap by testing M&A activity as a catalyst for corporate culture transformation.

2.2. The Rise of ESG Culture

As discussed earlier, corporate culture has been studied in many academic fields for decades, through the lenses of leadership, governance, financial performance, and more. But the recent rise of ESG has added a new dimension to this analysis: one that includes sustainability and

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[884] *See* John W. Meyer & Brian Rowan, *Institutionalized Organizations: Formal Structure as Myth and Ceremony*, 33 AM. J. SOCIOL. 95, 102 (1977).

[885] *Id.*

[886] *See, e.g., On The Rise: Navigating The Wave of Greenwashing and Social Washing,* REPRISK (Oct. 2023), https://www.reprisk.com/research-insights/reports/on-the-rise-navigating-the-wave-of-greenwashing-and-social-washing (last visited Jan. 20, 2025).

[887] *See* Kotter, *supra* note 50.

[888] *See* Agency Staff, *Rockstar Games Cleaned Up Its Toxic Culture – and Grand Theft Auto, Too*, *TechCentral* (July 28, 2022), https://techcentral.co.za/rockstar-games-cleaned-up-its-toxic-culture-and-grand-theft-auto-too/213664/ (explaining the efforts of the firm to change its toxic corporate culture).

stakeholder interests as part of a company's identity and purpose. ESG is currently seen as an organization's commitment to sustainability for long-term value creation.[889] An increasingly important part of the corporate culture is how companies consider social and environmental aspects into their daily operations and interactions and decision making, which constitute their ESG culture. As part of the process of considering their stakeholders' interests, firms often communicate with them about their vision, mission, and values by reporting ESG practices.[890] Furthermore, companies frequently receive inputs from their key stakeholders,[891] and their resulting policies "reflect shared beliefs and values within an organization, defining corporate culture."[892]

However, ESG has not always been associated with sustainable business practices; it has, indeed, emerged as an investment screening tool.[893] The roots of ESG trace back to the Socially Responsible Investment (SRI) movement, which gained traction in the 1960s and 1970s as a way for investors to align their investment decisions with ethical principles.[894] SRI applied exclusion criteria to avoid investments in industries such as tobacco, firearms, or companies operating under apartheid regimes.[895] Even though effective in promoting ethical investment, SRI was largely viewed as a values-based approach that lead investors to make sacrifices on the financial side for

[889] *Id.*

[890] *See* GOV. & ACCT. INST., INC., *2024 Sustainability Reporting in Focus*, https://www.ga-institute.com/research/research/sustainability-reporting-trends/2024-sustainability-reporting-in-focus/ (last visited Mar. 15, 2025) (finding that a record 93% of Russell 1000 companies published a sustainability report in 2023 - an increase from 90% in 2022).

[891] *See, e.g.,* Gadinis & Miazad, *supra* note 60.

[892] *See* Frederick Bereskin, Suk Joon K. Byun, Micah S. Officer & J. Manuel Oh, *The Effect of Cultural Similarity on Mergers and Acquisitions: Evidence from Corporate Social Responsibility*, 53 J. FIN. & QUANT. ANAL. 1995 (2018). *See also* Chun-Keung (Stan) Hoi, Qiang Wu & Hao Zhang, *Is Corporate Social Responsibility (CSR) Associated with Tax Avoidance? Evidence from Irresponsible CSR Activities*, 88 ACCT. REV. 2025 (2013); Feng Gao, Ling Lei Lisic & Ivy Xiying Zhang, *Commitment to Social Good and Insider Trading*, 57 J. ACCT. & ECON. 149 (2014).

[893] *See, e.g.,* Elizabeth Pollman, *The Making and Meaning of ESG*, 14 HARV. BUS. L. REV. 403, 417–18 (2024), U. OF PA., INST. FOR LAW & ECON. RESEARCH PAPER NO. 22-23, EUR. CORP. GOVERNANCE INST.– LAW WORKING PAPER NO. 659/2022 (2022), https://ssrn.com/abstract=4219857 (last visited Mar. 16, 2025) (explaining the evolution of ESG).

[894] *See* Marina Welker & David Wood, *Shareholder Activism and Alienation*, 52 CURRENT ANTHROPOLOGY (2011), https://www.journals.uchicago.edu/doi/full/10.1086/656796 (tracing the history of the SRI movement).

[895] *See, e.g.,* ANN C. LOGUE. SOCIALLY RESPONSIBLE INVESTING FOR DUMMIES 96 (Wiley 2009).

moral purposes.[896] The early 2000s witnessed the evolution of ESG as investors started to incorporate sustainability into financial analysis. The turning point came in 2004 when the United Nations Global Compact released the Who Cares Wins report, which coined the term ESG as a tool for examining business sustainability and financial stability.[897] The report argued that the integration of ESG factors into financial analysis, asset management, and securities brokerage is crucial for long-term investment value, as these are material concerns. The subsequent launch of the Principles for Responsible Investment (PRI) in 2006 formalized ESG further,[898] encouraging global investors to implement environmental, social, and governance factors into portfolio management strategies.

Institutional investors such as BlackRock, Vanguard, and State Street were instrumental in the advance of ESG, by compelling publicly listed firms to engage in more extensive sustainable actions.[899] BlackRock CEO Larry Fink's annual letters to CEOs emphasized the need for companies to demonstrate a long-term commitment to sustainability, noting that ESG considerations were essential for corporate resilience and risk management.[900] State Street named "corporate culture" its top engagement priority for 2019, arguing that a "flawed corporate culture has resulted in high-profile cases of excessive risk-taking or unethical behaviors that negatively

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[896] *See, e.g.,* John H. Langbein & Richard A. Posner, *Social Investing and the Law of Trusts*, 79 MICH. L. REV. 72 (1980); Maria O'Brien Hylton, *Socially Responsible Investing: Doing Good Versus Doing Well in An Inefficient Market*, 42 AM. U. L. REV. 1 (1992). For the differences between SRI and ESG, *See* Blaine Townsend, *From SRI to ESG: The Origins of Socially Responsible and Sustainable Investing*, 1 J. IMPACT & ESG INVESTING 1 (2020); Max M. Schanzenbach & Robert H. Sitkoff, *Reconciling Fiduciary Duty and Social Conscience: The Law and Economics of ESG Investing By a Trustee*, 72 STAN. L. REV. 381 (2020); DAVID VOGEL, THE MARKET FOR VIRTUE: THE POTENTIAL AND LIMITS OF CORPORATE SOCIAL RESPONSIBILITY 3-4 (Brookings Inst. Press 2005).

[897] *See* UNITED NATIONS GLOBAL COMPACT, *Who Cares Wins: Connecting Financial Markets To A Changing World* (Int'l Fin. Corp. & Swiss Fed. Dep't of Foreign Affs. 2004), https://documents1.worldbank.org/curated/en/444801491483640669/pdf/113850-BRI-IFC-Breif-whocares-PUBLIC.pdf (last visited Mar. 15, 2025).

[898] *See* UNITED NATIONS PRINCIPLES FOR RESPONSIBLE INVESTMENT (PRI), *A Blueprint for Responsible Investment* (2006), https://www.unpri.org/about-us/a-blueprint-for-responsible-investment (last visited Mar. 15, 2025).

[899] *See, e.g.,* Letter from Larry Fink, CEO, BlackRock, to CEOs, *A Sense of Purpose*, BLACKROCK (2018), https://www.blackrock.com/corporate/investor-relations/2018-larry-fink-ceo-letter (last visited Mar. 15, 2025).

[900] *Id.*

impact long-term performance."[901] Sixty percent (60%) of Vanguard's engagements with companies during 2020 covered board composition and diversity discussion, issues that fall under the broader ESG umbrella.[902]

The transformation of ESG from an investment screening tool to a broader paradigm for sustainable business initiatives was further triggered by the Business Roundtable's 2019 new statement for corporate purpose.[903] Historically, the Business Roundtable has advocated shareholder primacy, or that corporations exist primarily for the shareholders' benefit. But in what was considered a paradigm shift, 181 CEOs signed a statement redefining the corporation's purpose to include a commitment to customers, employees, suppliers, and communities, alongside shareholders.[904]

Subsequent regulatory developments then helped to mainstream ESG. While ESG remains largely voluntary in many jurisdictions, regulators are increasingly requiring sustainability disclosure from companies.[905] The European Union's Corporate Sustainability Reporting Directive (CSRD) exemplifies this shift, mandating standardized environmental and social disclosures to enhance corporate transparency and accountability. The Corporate Sustainability Due Diligence Directive (CSDDD or C3D) goes even further, mandating human rights due diligence in supply chains for large companies operating in the European market.[906] In the United States, the Securities

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[901] *See* Cyrus Taraporevala, *2019 Proxy Letter – Aligning Corporate Culture with Long-Term Strategy*, STATE ST. GLOB. ADVISORS (Jan. 15, 2019), https://corpgov.law.harvard.edu/2019/01/15/2019-proxy-letter-aligning-corporate-culture-with-long-term-strategy/ (last visited Mar. 15, 2025).

[902] *See* VANGUARD, *Investment Stewardship: 2020 Annual Report* (12 Months Ended Dec. 31, 2020), 5, https://about.vanguard.com/investment-stewardship/perspectives-and-commentary/2021_investment_stewardship_annual_report.pdf (last visited Mar. 15, 2025).

[903] *See* BUSINESS ROUNDTABLE, *Business Roundtable Redefines the Purpose of a Corporation to Promote 'An Economy That Serves All Americans'* (Aug. 19, 2019), https://www.businessroundtable.org/business-roundtable-redefines-the-purpose-of-a-corporation-to-promote-an-economy-that-serves-all-americans (last visited Mar. 15, 2025).

[904] *Id.*

[905] *See* EUROPEAN COMMISSION, *Corporate Sustainability Reporting Directive (CSRD)*, https://finance.ec.europa.eu/capital-markets-union-and-financial-markets/company-reporting-and-auditing/company-reporting/corporate-sustainability-reporting_en (last visited Mar. 16, 2025).

[906] *See* EUROPEAN COMMISSION, *Corporate Sustainability Due Diligence Directive*, https://commission.europa.eu/business-economy-euro/doing-business-eu/sustainability-due-diligence-responsible-business/corporate-sustainability-due-diligence_en (last visited Aug. 2, 2025) (explaining CSDDD obligations and scope).

and Exchange Commission (SEC)'s climate disclosure rules[907] and the California climate laws[908] also show these regulatory aspirations, despite ongoing legal challenges in court.[909] The International Sustainability Standards Board (ISSB),[910] in turn, represents a development beyond the "Brussels Effect,"[911] emerging as the global baseline for convergence in sustainability disclosure standards.[912]

The rise of ESG as shorthand for sustainable business practices did not occur in a vacuum. It emerged after decades of Corporate Social Responsibility (CSR) practices, which led businesses to adopt ethical business and community support.[913] Though CSR and ESG share similar objectives, they differ in scope and implementation. CSR is traditionally viewed as a voluntary initiative focused on philanthropy, employee welfare, and corporate integrity.[914] The majority of CSR programs were corporate giving and social projects without the integration of sustainability

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[907] *See* U.S. SEC. & EXCH. COMM'N, *SEC Finalizes Rules to Enhance and Standardize Climate-Related Disclosures for Investors* (Mar. 6, 2024), https://www.sec.gov/newsroom/press-releases/2024-31 (last visited Mar. 16, 2025). *See, e.g.,* Nick Grabar, Lillian Tsu & Helena Grannis, *SEC's Climate Disclosure Rules: GHG Emissions Disclosure Requirements*, HARV. L. SCH. F. ON CORP. GOVERNANCE (May 6, 2022), https://corpgov.law.harvard.edu/2022/05/06/secs-climate-disclosure-rules-ghg-emissions-disclosure-requirements/ (last visited Feb. 6, 2025).

[908] *See* CAL. AIR RES. BD., *Information Solicitation to Inform Implementation of California Climate-Disclosure Legislation: Senate Bills 253 and 261, as Amended by SB 219* (Dec. 16, 2024), https://ww2.arb.ca.gov/sites/default/files/2024-12/ClimateDisclosureQs_Dec2024.pdf (last visited Mar. 16, 2025).

[909] *See* Matthew Goldstein, *S.E.C. Moves to Kill Climate Disclosure Rule*, N.Y. TIMES (Feb. 11, 2025), https://www.nytimes.com/2025/02/11/us/politics/sec-climate-disclosure-rule.html (last visited Mar. 16, 2025); DAVIS POLK & WARDWELL LLP, *California's Climate-Related Disclosure Laws Clear First Litigation Hurdle* (Nov. 21, 2024), https://www.davispolk.com/insights/client-update/californias-climate-related-disclosure-laws-clear-first-litigation-hurdle (last visited Mar. 16, 2025).

[910] *See* INT'L SUSTAINABILITY STANDARDS BD., *IFRS S1 General Requirements for Disclosure of Sustainability-related Financial Information* (June 26, 2023), https://www.ifrs.org/issued-standards/ifrs-sustainability-standards-navigator/ifrs-s1-general-requirements/; INT'L SUSTAINABILITY STANDARDS BD., *IFRS S2 Climate-related Disclosures* (June 26, 2023), https://www.ifrs.org/issued-standards/ifrs-sustainability-standards-navigator/ifrs-s2-climate-related-disclosures/.

[911] *See* ANU BRADFORD, THE BRUSSELS EFFECT: HOW THE EUROPEAN UNION RULES THE WORLD (Oxford Univ. Press 2020).

[912] *See generally,* Stavros Gadinis & Silvia Fregoni, *Beyond the Brussels Effect: The Surprising Rise of the International Sustainability Standards Board*, J. INT'L ECON. L. (forthcoming 2025) (manuscript on file with authors).

[913] *See, e.g.,* Pollman, *supra* note76.

[914] *Id.*

into business processes.[915] ESG, however, is concerned with quantifiable and material sustainability practices.[916] It is, arguably, the "business case" for sustainability. While firms were able to pursue CSR at their discretion, ESG now constitutes an institutionalized set of practices that investors, regulators, and stakeholders monitor.[917]

Despite increasing adoption of ESG, translating corporate commitments into action continues to be a challenge. One of the largest concerns is greenwashing, where companies publicly support ESG initiatives but do not effectively integrate them into their strategies. Greenwashing appears in various forms, including misleading claims, selective disclosure of ESG factors, and promises without measurable action.[918] The recent surge in ESG litigation highlights the risks associated with greenwashing. Companies that pledge ambitious climate targets without a plan for achieving that have been brought to court by investors and consumers.[919] And, so far, greenwashing are among the most successful types of climate change lawsuits.[920]

Additionally, ESG has faced significant backlash in the last two years, particularly in the United States. Conservative groups argue that ESG is a shift from the shareholder primacy that dominated American businesses for decades and should, therefore, be resisted.[921] This criticism is

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[915] *See* Archie B. Carroll, *Corporate Social Responsibility: Evolution of a Definitional Construct*, 38 BUS. & SOC'Y 268 (1999).

[916] *See* Pollman, *supra* note 76.

[917] *See* Peter Reali, Jennifer Grzech & Anthony Garcia, ESG: *Investors Increasingly Seek Accountability and Outcomes*, HARV. L. SCH. F. ON CORP. GOVERNANCE (Apr. 25, 2021), https://corpgov.law.harvard.edu/2021/04/25/esg-investors-increasingly-*See*k-accountability-and-outcomes/ (last visited Mar. 16, 2025) (discussing how investors were using proxy votes to express their views on company social and environmental behavior, rather than relying on company disclosure).

[918] *See, e.g.,* Célia Santos, Arnaldo Coelho & Alzira Marques, *A Systematic Literature Review on Greenwashing and Its Relationship to Stakeholders: State of Art and Future Research Agenda*, 74 MGMT. REV. Q. 1397 (2024), https://doi.org/10.1007/s11301-023-00337-5 (last visited Mar. 16, 2025).

[919] *See* Joana Setzer & Catherine Higham, *Global Trends in Climate Change Litigation: 2024 Snapshot*, LSE GRANTHAM INST. ON CLIMATE CHANGE & THE ENV'T (June 2024), https://www.lse.ac.uk/granthaminstitute/wp-content/uploads/2024/06/Global-trends-in-climate-change-litigation-2024-snapshot.pdf (last visited Mar. 16, 2025).

[920] *See* Juliana Vélez-Echeverri, Catherine Higham & Joana Setzer, *Climate-Washing Litigation: Towards Greater Corporate Accountability*, GRANTHAM RSCH. INST. ON CLIMATE CHANGE & ENV'T, LONDON SCH. ECON. & POL. SCI. (Oct. 2023), https://www.lse.ac.uk/granthaminstitute/news/climate-washing-litigation-towards-greater-corporate-accountability/.

[921] *See, e.g.,* Kiara Alfonseca, *What Does 'Woke' Mean, and Why Are Some Conservatives Using It?*, ABC NEWS (Nov. 14, 2022), https://abcnews.go.com/Politics/woke-conservatives/story?id=93051138 (last visited Mar. 15, 2025).

generally situated within broader ideology battles, in which ESG is attacked as an extension of "woke capitalism"—a term that initially derived from the social justice movement but has been taken over in politics to refer to corporate initiatives viewed as too liberal like the stakeholder governance.[922] As part of this backlash, several states have enacted restrictions on pension funds, prohibiting them from considering ESG factors in investment decisions.[923] Meanwhile, courts have increasingly been asked to hear challenges to corporate Diversity, Equity, and Inclusion (DEI) policies.[924] Despite these challenges, ESG continues to be central to the business and law discussion and will likely continue like this, even if rebranded, as regulations spread globally. Therefore, studying ESG practices' impacts as well as their implementation, change and evolution over time is crucial.

The literature has identified multiple internal and external determinants of ESG culture across organizations.[925] One internal determinant is corporate governance. Research has linked effective governance structures, such as diverse and independent boards, to higher ESG performance.[926] Another determinant is leadership commitment, as top managers prioritizing sustainability often drive stronger ESG outcomes. This is consistent with great part of the corporate

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[922] *See, e.g.,* Domenico Montanaro, *What Does the Word 'Woke' Really Mean, and Where Does It Come From?,* NPR (Jul. 19, 2023), https://www.npr.org/2023/07/19/1188543449/what-does-the-word-woke-really-mean-and-where-does-it-come-from (last visited Mar. 15, 2025) (exploring the historical context and transformation of the term "woke," from its roots in African American Vernacular English, signifying awareness of social injustices, to its contemporary usage in political and cultural discussions).

[923] *See, e.g.,* Joshua A. Lichtenstein et al., *The New Battleground in the Fight over ESG's Role in Public Pension Investments: The Courtroom*, ROPES & GRAY VIEWPOINTS (Nov. 5, 2024), https://www.ropesgray.com/en/insights/viewpoints/102jniy/the-new-battleground-in-the-fight-over-esgs-role-in-public-pension-investments (last visited Mar. 3, 2025).

[924] *See, e.g.,* Mike Delikat & Ernan Kiselica, *Litigation Targeting Large Company DEI Programs on the Rise*, HARV. L. SCH. F. ON CORP. GOVERNANCE (Sept. 18, 2024), https://corpgov.law.harvard.edu/2024/09/18/litigation-targeting-large-company-dei-programs-on-the-rise/ (last visited Mar. 3, 2025).

[925] *See* Alice Martiny, Jonathan Taglialatela, Francesco Testa & Fabio Iraldo, *Determinants of Environmental Social and Governance (ESG) Performance: A Systematic Literature Review*, **J. CLEAN. PROD.** (2024), https://doi.org/10.1016/j.jclepro.2024.140916.

[926] *See, e.g.,* Siyu Meng, Hongli Su & Jing Yu, *Digital Transformation and Corporate Social Performance: How Do Board Independence and Institutional Ownership Matter?*, 13 FRONT. PSYCHOL., Aug. 2022, https://doi.org/10.3389/fpsyg.2022.915583 (finding that board independence and institutional ownership positively influence corporate social performance in the context of digital transformation); Marios Nerantzidis, Panagiotis Tzeremes, Andreas Koutoupis & Antonios Pourgias, *Exploring the Black Box: Board Gender Diversity and Corporate Social Performance*, 48 FIN. RES. LETT. 102987 (2022), https://doi.org/10.1016/j.frl.2022.102987 (showing that greater board gender diversity is associated with improved corporate social performance).

culture literature that believes that the tone comes from the top.[927] Additionally, company characteristics, such as firm size, financial performance, and industry sector, are considered internal factors that influence ESG initiatives.[928] For example, wealthier companies (the ones with better financial performance) would have more financial resources and personnel to support the implementation of sustainability practices than less-resourced firms.

On the side of external determinants of ESG, studies have appointed the regulatory environment as an important driver: tight rules induce companies to enhance their ESG practices.[929] In the same way, stakeholder pressure, including demand from investors, customers, and NGOs, is seen as an external determinant that can motivate firms to improve their ESG performance.[930] Finally, macroeconomic shocks and economic developments are also among external determinants, as the context in which a company operates can influence its approach to environmental and social aspects.[931] While M&A activity is not often singled out as an ESG driver,

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[927] *See, e.g.,* Luke Crace & Joel Gehman, *What Really Explains ESG Performance? Disentangling the Asymmetrical Drivers of the Triple Bottom Line*, 36 ORG. & ENV'T 150 (2022), https://doi.org/10.1177/10860266221079408 (identifying asymmetrical internal and external drivers of environmental, social, and governance performance); Jordi Garcia-Blandon, Josep M. Argilés-Bosch & Daniele Ravenda, *Exploring the Relationship Between CEO Characteristics and Performance*, 20 J. BUS. ECON. MGMT. 1064 (2019), https://doi.org/10.3846/jbem.2019.10447 (finding that CEO characteristics significantly influence firm performance).

[928] *See, e.g.,* Stefanie Drempetic, Christian Klein & Bernhard Zwergel, *The Influence of Firm Size on the ESG Score: Corporate Sustainability Ratings Under Review*, 167 J. BUS. ETHICS 333 (2020), https://doi.org/10.1007/s10551-019-04164-1 (finding that larger firms tend to receive higher ESG ratings, in part due to greater resources and disclosure capacity). *See also* Martiny et al., *supra* note 108.

[929] *See* Helena Ahlström & Domenico Monciardini, *The Regulatory Dynamics of Sustainable Finance: Paradoxical Success and Limitations of EU Reforms*, 177 J. BUS. ETHICS 193 (2022), https://doi.org/10.1007/s10551-021-04763-x (examining the successes and shortcomings of recent EU sustainable finance reforms, including their implications for corporate ESG practices).

[930] *See, e.g.,* Byung-Cheol Yoo, *Exploring Stakeholder and Organizational Influences on ESG Engagement in Logistics*, SUSTAINABILITY (2025), https://doi.org/10.3390/su17094243 (finding investor and customer pressures to be among the most influential forces shaping firms' ESG practices); Seow Ting Lee & Daniel Riffe, *Who Sets the Corporate Social Responsibility Agenda in the News Media? Unveiling the Agenda-Building Process of Corporations and a Monitoring Group*, 43 PUB. REL. REV. 293 (2017), https://doi.org/10.1016/j.pubrev.2017.02.007 (examining how corporations and monitoring groups influence media coverage of corporate social responsibility issues).

[931] *See* Laurence Cassely, Souad Larbi, Christophe Revelli & Arnaud Lacroux, *Corporate Social Performance (CSP) in Time of Economic Crisis*, 12 SUSTAINABILITY ACCT., MGMT. & POL'Y J. 913 (2021), https://doi.org/10.1108/SAMPJ-07-2020-0262 (analyzing the resilience and drivers of corporate social performance during periods of economic crisis); Heikki Arminen, Kai Puumalainen, Sanna Pätäri & Katharina Fellnhofer, *Corporate Social Performance: Inter-Industry and International Differences*, 177 J. CLEAN. PROD. 426 (2017), https://doi.org/10.1016/j.jclepro.2017.12.250 (comparing CSP performance across industries and countries, identifying structural and contextual determinants).

I argue that these deals can be significant catalysts for ESG culture change, as discussed in Part 3 of this paper.[932]

2.3. Connecting ESG Culture and M&A Activity

After conceptualizing corporate culture and the rise of ESG culture, this section examines how these areas relate to M&A activity, which is the baseline scenario for this research. M&A transactions represent one of the most significant strategic tools for external corporate growth, enabling firms to achieve economies of scale, expand market share, and gain new capabilities.[933] M&A has a long history, particularly in the United States and Europe, and some scholars acknowledge waves of such activity since the early 1900s.[934] The transactions involve an impressive amount of financial resources, with global M&A deal value expected to reach $3.5 trillion in 2024.[935] M&A success is primarily attributed to the synergy gains achieved during the post-merger integration process.[936] While financial, regulatory, and operational concerns have traditionally been seen as determinants of M&A outcomes, corporate culture has emerged as another critical factor for post-deal success.[937] Synergy advantages that companies seek from M&A are not only a result of financial and operational integration but also cultural alignment among the

[932] *See infra* Part 3.

[933] *See, e.g.,* Franz Bauer & Kurt Matzler, *Antecedents of M&A Success: The Role of Strategic Complementarity, Cultural Fit, and Degree and Speed of Integration*, 35 STRATEGIC MGMT. J. 269, 269–91 (2014).

[934] *See, e.g.,* Marina Martynova & Luc Renneboog, *The Performance of the European Market for Corporate Control: Evidence from the 5th Takeover Wave*, EUR. FIN. MGMT. J. (forthcoming), ECGI – FIN. WORKING PAPER NO. 135/2006, CENTER DISCUSSION PAPER NO. 2006-118 (2008), https://ssrn.com/abstract=941731 (last visited Mar. 16, 2025).

[935] *See* BAIN & COMPANY, *Global M&A Deal Value on Track to Reach $3.5 Trillion in 2024 (2024*), https://www.bain.com/about/media-center/press-releases/2024/global-ma-deal-value-on-track-to-reach-$3.5-trillion-in-2024bain--company (last visited Mar. 16, 2025).

[936] *See* Bereskin et al., *supra* note 75.

[937] *See, e.g.,* Bauer Florian & Matzler Kurt, *Antecedents of Mergers and Acquisitions Performance: The Role of Strategic Complementarity, Cultural Fit, and Degree of Integration*, 45 STRAT. MGMT. J. 432, 436 (2014).

companies..[938] Without cultural alignment, mergers that theoretically are strategically sound do not realize their benefits.[939]

Empirical studies support the significance of cultural fit in M&A selection. In a survey among executives, 54% said they would walk away from a culturally misaligned M&A target, and an additional third responded that they would discount the target's valuation by 10% to 30% due to cultural reasons.[940] Another study reported that 61% of interviewed executives considered corporate culture to be at least as influential as financial issues in M&A success.[941] Later studies linked the "organizational fit" directly to the post-merger performance of the acquirer.[942]Such findings suggest that corporate culture is more than an aspect to take care after the deal occurs; it is, in fact, a key issue in assessing the viability of a transaction.[943]

Several high-profile merger failures illustrate the dangers of cultural problems. The deals of Sprint and Nextel, MCI and WorldCom, AOL and Time Warner, Citigroup and Travelers, HP, and Compaq, Daimler and Chrysler have all been cited as examples where cultural incompatibility contributed to integration problems and disappointing financial performance.[944] In many of these examples, differences in culture led to internal conflicts and difficulty in getting strategic priorities in place, and, in a few cases, the eventual collapse of the merger.[945] A more recent example is

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[938] *See, e.g.,* Bereskin et al., *supra* note 75.

[939] *Id.*

[940] *See* Grennan et al., *supra* note 30.

[941] *See* Schein, *supra* note 29, at 22.

[942] *See* Deepak K. Datta, *Organizational Fit and Acquisition Performance: Effects of Post-Acquisition Integration*, 12 STRAT. MGMT. J. 281, 285 (1991)

[943] *See* Alan Lewis & Dan McKone, *So Many M&A Deals Fail Because Companies Overlook This Simple Strategy*, HARV. BUS. REV. (May 10, 2016), https://hbr.org/2016/05/so-many-ma-deals-fail-because-companies-overlook-this-simple-strategy (last visited Mar. 16, 2025) (saying that more than half of all mergers destroy shareholder value).

[944] *See, e.g.,* Rana Foroohar, *Culture Clashes Loom After a Rush of Company Mergers*, FIN. TIMES (Jul. 8, 2018), https://www.ft.com/content/633dcfba-810a-11e8-bc55-50daf11b720d (last visited Mar. 16, 2025); Sydney Finkelstein, *The DaimlerChrysler Merger*, TUCK SCH. OF BUS. CASE STUDY No.. 1-0071 (2002) (analyzing the cultural and strategic challenges that contributed to the failure of the DaimlerChrysler merger); *How the AOL-Time Warner Deal Went Wrong*, N.Y. TIMES DEALBOOK (Jan. 11, 2010), http://dealbook.nytimes.com/2010/01/11/how-the-aol-time-warner-deal-went-wrong/ (last visited Mar. 16, 2025) (examining the failed AOL-Time Warner merger, highlighting strategic misalignment, cultural clashes, and the impact of unrealistic synergies on the deal's collapse).

[945] *See* ROBERT F. BRUNER, DEALS FROM HELL: M&A LESSONS THAT RISE ABOVE THE ASHES 78 (2004).

Bayer's 2018 acquisition of the American Monsanto. The German pharmaceutical and chemical company spent two years navigating global antitrust scrutiny[946] to finalize the $63 billion acquisition, the largest in its history.[947] However, Monsanto's reputation, particularly linked to its herbicide product Roundup, and the litigation it faced over environmental and health concerns triggered significant backlash. Shortly after the deal closed, Bayer was hit with a wave of lawsuits and public protests, and within a year, the transaction was widely regarded as one of the worst corporate deals in recent memory.[948] By 2019, Bayer's market capitalization had dropped by nearly the entire value it paid for Monsanto, meaning the value of an entire company had almost entirely evaporated.[949]

Empirical studies in this area, conducted mainly by finance scholars, are primarily concerned with investigating how corporate culture influences post-merger outcomes, like in the examples above. Cultural differences between merging companies have been associated with higher agency costs,[950] loss of trust, and polarization of management teams,[951] for example. When executives and employees at the target company are resistant to integration due to different cultures, productivity declines and inefficiencies in decision-making arise.[952] It has been established that cultural incompatibility is one of the top reasons M&A fails, with merging companies usually failing to achieve expected synergies due to the inability to combine disparate corporate cultures.[953]

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[946] *See, e.g.,* Chad Bray, *Bayer-Monsanto Deal Faces Deeper Scrutiny in Europe*, N.Y. TIMES, (Aug. 22, 2017), https://www.nytimes.com (last visited Feb. 6, 2024).

[947] *See, e.g.,* Jeff Daniels, *Germany's Bayer Closes $63 Billion Monsanto Takeover, Plans to Drop U.S. Company's Name*, CNBC (June 7, 2018), https://www.cnbc.com (last visited Feb. 6, 2024).

[948] *See, e.g.,* Ruth Bender, *Bayer's Roundup Problem Slashes Its Market Value*, WALL ST. J. (May 19, 2019), https://www.wsj.com/articles/bayers-roundup-woes-send-investors-fleeing-11558266059 (last visited Feb. 6, 2024).

[949] *Id.*

[950] *See* Eric Van den Steen, *Culture Clash: The Costs and Benefits of Homogeneity in Mergers*, 34 J. FIN. ECON. 92, 95 (2010).

[951] *See* Paul Shrivastava, *Postmerger Integration*, 7 J. BUS. STRAT. 65, 69 (1986).

[952] *See* Datta, *supra* note 125, at 290.

[953] *See* Susan Cartwright & Cary Cooper, *The Role of Culture Compatibility in Successful Organizational Marriage*, 13 ACAD. MGMT. EXEC. 75, 78 (1993).

One of the most problematic consequences of cultural misfits in M&A is the loss of valuable employees. Studies have indicated that employee turnover is a consequence of some mergers, particularly when employees of the acquired firm realize a mismatch between their proven workplace culture and the new organizational structure.[954] This experience is most dramatic in knowledge-intensive industries, such as finance and information technology, in which human capital is essential to the creation of value. Failure to retain top talent after a merger may undermine those competitive strengths that initially motivated the transaction.[955] Cross-border M&A deals involve other cultural challenges, including executives coping with differences in labor laws, employee expectations, and corporate governance practices that may not necessarily surface until the due diligence stage.[956]

Given the challenges resulting from cultural misalignment, there is a growing understanding of the importance of cultural due diligence for M&A transactions.[957] Research has shown that cultural misfits account for a great part of failed mergers and acquisitions,[958] so companies need to do an intensive cultural evaluation prior to deal closure.[959] Cultural due diligence involves an assessment of the target's organizational culture in order to identify probable integration issues and inform decision-making.[960] While conventional operational and financial due diligence addresses a company's operations, technology, or finances, cultural due diligence examines the values, leadership behaviors, communication practices, employee motivation, and

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[954] *Id.*

[955] *Id.*

[956] *See* George Alexandridis, Andreas Hoepner, Rongxin Huang & Ioannis Oikonomou, *Cross-Border Mergers and National Cultural Differences*, 69 J. INT'L BUS. STUD. 51, 56 (2015).

[957] *See* Richard S. Ruback & Michael C. Jensen, *The Market for Corporate Control: The Scientific Evidence*, 11 J. FIN. ECON. 5, 9 (1983).

[958] *See* Alan Lewis & Dan McKone, *So Many M&A Deals Fail Because Companies Overlook This Simple Strategy*, HARV. BUS. REV. (May 10, 2016), https://hbr.org/2016/05/so-many-ma-deals-fail-because-companies-overlook-this-simple-strategy (last visited Mar. 16, 2025) (saying that more than half of all mergers destroy shareholder value).

[959] *See* Jean-François Hennart & Sabine Reddy, *The Impact of Cultural Differences on Acquisitions: A Case Survey of 40 French and German Acquisitions*, 12 INT'L BUS. REV. 111, 117 (2002).

[960] *See* DANIEL DENISON & WILLIAM KO, CULTURAL DUE DILIGENCE IN MERGERS AND ACQUISITIONS 3 (Denison Consulting 2019), https://denisonconsulting.com/wp-content/uploads/2019/05/culturalduediligence-denisonko.pdf.

overall organizational norms and values.[961] Effective cultural analysis allows acquiring companies to anticipate probable conflict and create integration approaches that create alignment rather than resistance.[962] Recent research identified the changing dynamics of cultural due diligence, especially in the post-COVID-19 world.[963] Remote working has added complexity to the classic approaches to due diligence, making it harder to evaluate a target firm's workplace culture and relationship dynamics.[964] Firms have had to increasingly depend on digital equipment, virtual sessions, and AI-powered cultural analytics to fill the gaps.[965]

ESG's key position in recent years has prompted scholars to also investigate the specific role of ESG culture in M&A deals. These studies are primarily focused on a few areas. One is the ESG effect on the acquirer's market performance in the short term, that is, whether ESG-aware acquirers achieve higher merger announcement returns.[966] These studies indicate that acquiring firms with well-established ESG cultures often receive positive stock market reactions because investors perceive them as more resilient, more strategically sustainable, and better equipped for integration challenges.[967] ESG-conscious acquirers may also benefit from higher investor confidence, leading to subsequent superior financial performance after the deal.[968]

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[961] *See* Boris Groysberg et al., *The Leader's Guide to Corporate Culture*, HARV. BUS. REV. (Jan.-Feb. 2018), https://hbr.org/2018/01/the-culture-factor (last visited Mar. 5, 2025).

[962] *See* PHILIPPE HASPESLAGH & DAVID JEMISON, MANAGING ACQUISITIONS: CREATING VALUE THROUGH CORPORATE RENEWAL 56 (1991); Jeffrey Krug, *Why Mergers Fail: An Integrative Framework*, 31 ACAD. MGMT. PERSP. 136, 138 (2017).

[963] *See* Frank J. Schmidt, *Post-Pandemic Cultural Due Diligence in M&A: Challenges and Strategies*, SSRN (Feb. 2021), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3798057.

[964] *See* Anup Srivastava & Preetika Joshi, *M&A Due Diligence in the Digital Age: The Role of AI and Big Data*, 49 J. CORP. FIN. 112, 119 (2022).

[965] *See, e.g., AI-Powered Cultural M&A Diligence Analysis*, DELOITTE, https://www2.deloitte.com/us/en/blog/mergers-acquisitions-insights-news/2024/ai-powered-cultural-m-and-a-diligence-analysis.html (last visited Mar. 18, 2025).

[966] *See* e.g., Xin Deng, Jun-Koo Kang & Buen Sin Low, *Corporate Social Responsibility and Stakeholder Value Maximization: Evidence from Mergers*, 110 J. FIN. ECON. 87 (2013); Tzu-Yi Yen & Paul André, *Market Reaction to the Effect of Corporate Social Responsibility on Mergers and Acquisitions: Evidence on Emerging Markets*, 71 Q. REV. ECON. & FIN. 114 (2019).

[967] *See* Daniel Krishnamurti, Howard Yen & Rui Qiao, *ESG Culture and Acquisition Returns: A Cross-Country Analysis*, 41 J. BUS. ETHICS 88, 92 (2019).

[968] *See* Brian D. Gomes, Patrick Qiao & Michael Lee, *Does ESG Culture Improve M&A Success? An Empirical Investigation*, 32 J. BUS. FIN. & ACCT. 235, 240 (2018).

Another key area of investigation is whether ESG culture influences the acquisition premiums paid to target firms.[969] Certain research shows that strong ESG-culture targets obtain better valuations since their sustainability commitments reduce operating risks and enhance value creation over the longer term.[970] However, empirical findings remain mixed. Some scholars found that ESG-aware targets might not necessarily have higher offer prices, questioning the hypothesis that a more robust ESG culture should naturally translate to higher M&A premiums.[971]

Besides the impact on market performance and deal valuation, ESG culture seems to play a role in minimizing M&A transaction risk, especially if there is an alignment between acquirer and target.[972] High ESG cultural fit firms are likely to experience fewer integration problems because shared sustainability values and governance norms make the transition smoother.[973] Some studies also show that ESG-aligned acquirers experience reduced deal completion uncertainty because their effective governance mechanisms reduce regulatory scrutiny, litigation risk, and reputation problems.[974]

While significant focus has been on the impact of ESG culture on M&A outcomes, there is a surprising lack of research in the opposite direction: how M&A deals influence the ESG culture of the acquirer company.[975] It is unclear how ESG culture evolves following M&A transactions, particularly when acquirers and targets have divergent sustainability priorities. Some acquirers may successfully incorporate ESG culture into post-merger organizational structures so that sustainability commitments continue to be at the heart of corporate decision-making, while others may be less successful in this endeavor, leading to inconsistency in the application of ESG and

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[969] *See* Julien Bereskin, Jin Hoepner & Rongxin Huang, *The ESG Culture Premium: Do Sustainable Firms Receive Higher Acquisition Offers?*, 25 J. EMPIRICAL FIN. 78, 83 (2018). (e.g., Gomes et al., 2018; Qiao et al., 2019)

[970] *See* George Alexandridis, Ioannis Oikonomou & Frederik Boone, *Cultural Alignment and M&A Performance: The Role of ESG Culture*, 14 REV. CORP. FIN. STUD. 165, 170 (2020); Denison & Ko, *supra* note 143.

[971] *See* Srivastava & Joshi, *supra* note 147.

[972] *See* Schmidt, *supra* note 146.

[973] *Id.*

[974] *See* SYDNEY FINKELSTEIN & JO WHITEHEAD, THINK AGAIN: WHY GOOD LEADERS MAKE BAD ESG DECISIONS AND HOW TO KEEP IT FROM HAPPENING TO YOU 127 (Harvard Bus. Rev. Press 2010).

[975] *See* ROBERT F. BRUNER, APPLIED MERGERS AND ACQUISITIONS: ESG INTEGRATION IN M&A 402 (John Wiley & Sons 2004).

even to ESG-washing risk.[976] Furthermore, there is limited evidence on whether firms that successfully retain an ESG culture in post-merger operations experience better long-term financial returns. As M&A transactions continue to reshape the world's business landscape, it remains relevant to know where ESG culture stands in deal-making.[977]

3. Theory and Hypothesis Development

The analysis of how M&A transactions impact ESG corporate culture involves mainly two literatures. The first is the literature that connects corporate culture with M&A deals. The second is the scholarship discussing shareholder versus stakeholder value creation. This paper explores both.

M&A are transformative corporate events that not only shape market positioning and financial performance but also serve as catalysts for cultural evolution. The integration of ESG considerations in corporate culture has increasingly become a focal point in M&A transactions. While extensive research has examined the impact of corporate culture on a variety of business outcomes,[978] there are just a few studies focusing on the other way around, which will be explored next. The ways in which ESG culture evolves post-merger remain particularly underexplored. Given the growing prominence of ESG as a determinant of corporate strategy, M&A presents a crucial setting to examine whether ESG culture is transmitted, diluted, or reshaped when two firms with different ESG profiles merge.

3.1. Culture Clash and Culture Synergy Theories

The research on corporate culture in the context of M&A suggests two opposing theoretical perspectives. The first is the "culture clash," which implies that the cultural difference between the

[976] *See* Boris Groysberg et al., *supra* note 144.

[977] *See infra* Part 4 (discussing the theories for the impact of M&A deals on ESG culture).

[978] *See supra* Part 2.3.

acquirer and target is an obstacle in the post-merger integration process, preventing the resulting firm of the deal from realizing the benefits of the acquisition.[979] Studies have documented that disparities in corporate culture and management styles create friction, leading to inefficient integration processes and lower post-merger performance.[980] Several others claim that great cultural distance often leads to more costs and higher risks in cross-cultural interactions.[981] Some also find that cultural misalignment is linked to increased agency costs and operational disruptions, all of which can weaken the long-term prospects of the merged entity.[982] For example, an empirical research on international M&A transactions showed that firms with substantial cultural differences experience greater integration challenges and, in some cases, lower cumulative abnormal returns (CAR) at the time of the merger announcement, suggesting that investors recognize the risks posed by cultural misalignment.[983] The greater the cultural distance, the higher the risk of failure, particularly in cross-border acquisitions, where national cultural differences further deepen organizational disparities and allow for fewer synergies.[984]

The second theory, the "culture synergy", argues that cultural differences do not necessarily impede post-merger performance but can instead facilitate learning, innovation, and

[979] For an economic theory of the costs and benefits of corporate culture homogeneity and the effects of "culture clash" in M&A, *See* Van den Steen, *supra* note 132, at 1718–1738 (showing that "shared beliefs lead to more delegation, less monitoring, higher utility (or satisfaction), higher execution effort (or motivation), faster coordination, less influence activities, and more communication, but also to less experimentation and less information collection"). *See also* KEVIN DAVID & HARBIR SINGH, *Sources of Acquisition Cultural Risk*, in THE MGMT. OF CORP. ACQUISITIONS 251, 251–92 (Gert-Jan M. H. van den Berg ed., Macmillan 1994); Anthony F. Buono, James L. Bowditch & John W. Lewis, *When Cultures Collide: The Anatomy of a Merger*, 38 HUM. REL. 477, 477–500 (1985); David M. Schweiger & Patricia K. Goulet, *Integrating Mergers and Acquisitions: An International Research Review*, 1 ADVANCES IN MERGERS & ACQUISITIONS 61, 61–91 (2000); Susan Cartwright & Richard Schoenberg, *Thirty Years of Mergers and Acquisitions Research: Recent Advances and Future Opportunities*, 17 BRIT. J. MGMT. 1, 1–5 (2006).

[980] *See, e.g.,* Sayan Chatterjee, Michael H. Lubatkin, David M. Schweiger & Yaakov Weber, *Cultural Differences and Shareholder Value in Related Mergers: Linking Equity and Human Capital*, 13 STRATEGIC MGMT. J. 319, 319–34 (1992); Datta, *supra* note 125.

[981] *See, e.g.,* GEERT HOFSTEDE, CULTURE'S CONSEQUENCES: INTERNATIONAL DIFFERENCES IN WORK-RELATED VALUES (Sage Pub'ns 1980).

[982] *See* Jensen & Meckling, *supra* note 2.

[983] *See* George Alexandridis, Andreas G. F. Hoepner, Zhijuan Huang & Ioannis Oikonomou, *The Impact of Corporate Cultural Distance on Mergers and Acquisitions*, EFM J. 1, 1–5 (2015).

[984] *Id.*

value creation.[985] This view suggests that acquisitions provide opportunities for knowledge transfer, organizational adaptation, and strategic renewal.[986] Closing a deal with a culturally distinct company can be a sign that the acquirer firm is willing to change and evolve. The acquirer may leverage these differences to introduce new capabilities and disrupt outdated practices.[987] The acquisition of a firm with distinct organizational values and operational frameworks can encourage an exchange of best practices, particularly when the acquirer demonstrates the ability to assimilate and adapt to the cultural attributes of the target.[988] Scholars also argue that acquisitions may broaden the firm's knowledge base, break inertia, and foster development through combinations of existing forms of knowledge.[989] However, differences between the organizations involved are only beneficial if they are not so large that the acquiring firm can no longer understand, absorb, and assimilate the target.[990]

As empirical studies on the theories report mixed results—sometimes supporting the culture clash theory and other times finding evidence of the culture synergy perspective—, the

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[985] *See, e.g.,* Jeffrey S. Harrison, Michael A. Hitt, Robert E. Hoskisson & R. Duane Ireland, *Synergies and Post-Acquisition Performance: Differences versus Similarities in Resource Allocations*, 17 J. MGMT. 173, 173–90 (1991) (arguing that cultural differences between merging firms can lead to value creation by providing opportunities for resource sharing and strategic renewal); Ingmar Björkman, Günter K. Stahl & Eero Vaara, *Cultural Differences and Capability Transfer in Cross-Border Acquisitions: The Mediating Roles of Capability Complementarity, Absorptive Capacity, and Social Integration*, 38 J. INT'L BUS. STUD. 658, 658–72 (2007) (suggesting that cultural differences can be leveraged to facilitate learning and innovation during the post-merger integration process); Hari A. Krishnan, Alex Miller & William Q. Judge, *Diversification and Top Management Team Complementarity: Is Performance Improved by Merging Similar or Dissimilar Teams?*, 18 STRATEGIC MGMT. J. 361, 361–74 (1997) (demonstrating that differences in functional backgrounds between top management teams of acquirers and targets can enhance post-acquisition performance).

[986] *See, e.g.,* Henrik Bresman, Julian Birkinshaw & Robert Nobel, *Knowledge Transfer in International Acquisitions*, 30 J. INT'L BUS. STUD. 439, 439–62 (1999) (highlighting that cultural differences can enhance post-merger integration by promoting knowledge transfer and organizational adaptation.). *See also* Riikka M. Sarala & Eero Vaara, *Cultural Differences, Convergence, and Crossvergence as Explanations of Knowledge Transfer in International Acquisitions,* 41 J. INT'L BUS. STUD. 1365 (2010) finding that cultural differences can provide potential for knowledge exchange in international acquisitions, reinforcing the notion that these differences may generate strategic benefits).

[987] *See, e.g.,* Björkman, Stahl & Vaara, *supra* note 168 (arguing that acquisitions involving culturally different firms can lead to new capabilities and learning-based innovation, which are key to strategic agility).

[988] *See* Bresman, Birkinshaw & Nobe*, supra* note 169 (supporting the idea that cultural differences, when managed effectively, foster an exchange of best practices).

[989] *See, e.g.,* Bruce Kogut & Udo Zander, *Knowledge of the Firm, Combinative Capabilities, and the Replication of Technology*, 3 ORG. SCI. 383, 383–397 (1992).

[990] *See* Freek Vermeulen & Harry Barkema, *Learning Through Acquisitions*, 44 ACAD. MGMT. J. 457, 457–476 (2001).

effects of cultural misalignment on M&A operations are still an open question. Both approaches will be the basis for this investigation into what happens to the ESG culture when two culturally different firms enter an M&A deal—whether it is the culture of the "good" company or the "bad" company that prevails. In other words, *whether the acquisition of a target that has higher or lower ESG culture than that of the acquirer in the premerger stage affects the ESG culture of the acquirer in the post-merger stage.*

Applying these theories to the ESG context, the culture clash perspective suggests that ESG misalignment between acquirers and targets will hinder ESG integration post-merger. Companies with different ESG cultures would experience a cultural collision in the post-merger period and, therefore, would find it challenging to integrate and benefit from the differences. In this way, if an acquirer with a lower ESG commitment acquires a target with a stronger ESG culture, the cultural misalignment may prevent the acquirer from adopting the sustainability principles of the target, leaving its ESG culture unchanged after the deal. Conversely, if an acquirer with a robust ESG culture acquires a firm with weaker ESG practices, one could expect the acquirer's ESG performance to be stable or even to decrease as a result of cultural challenges. The post-merger ESG culture of the acquirer may deteriorate as it struggles to impose its sustainability standards on the newly integrated entity. A study that corroborates the culture clash theory in the ESG framework is one carried out by Bereskin, Byon, Officer and Oh (2018), who analyzed KLD Research & Analytics CSR data and reported a positive relationship between sustainability similarity and announcement returns.[991]

This view is also consistent with the idea that corporate culture is often built from the top down.[992] A firm would not be able to change its ESG culture through an acquisition unless management deliberately chose to integrate the target's culture rather than suppress it. A top-down theory of corporate culture argues that a firm's culture begins with the CEO communicating the expected culture to all employees, who interpret the meaning of the message according to their personal perspectives and express their opinions to each other to arrive at a final inference of the

[991] *See* Bereskin et al., *supra* note 75.

[992] *See, e.g.,* George B. Gorton & Alexander K. Zentefis, *Corporate Culture as a Theory of the Firm* (NAT'L BUREAU OF ECON. RESEARCH, WORKING PAPER NO. 27353, 2020), https://ssrn.com/abstract=3626854; Schein, *supra* note 29.

culture intended by the CEO.[993] "Once team and corporate cultures are formed, they can be hard to change."[994] Another research suggest that corporate culture is shapeable by individuals, especially leaders, and that consequently, given normal personnel turnover, the culture will persist over time, evolving slowly if at all.[995]

Given the pivotal role of leaders in designing the corporate culture, they have gained attention from academics in the study of ESG. Research indicates that sustainability is more likely to succeed when CEOs and other corporate leaders set the right 'tone at the top' and operationalize ESG goals throughout the company.[996] That is why linking executive compensation to ESG goals is seen as a critical way to improve sustainability.[997] A recent study found, for example, that integrating environmental and social performance criteria into executive pay increases corporate ESG initiatives, reduces pollutant emissions, and increases green innovations.[998] According to this top-down theory of creating or changing corporate culture, acquiring a target with a superior ESG

[993] *See* Gorton & Zentefis, *supra* note 175.

[994] *Id.* at 8.

[995] *See* Hermalin, *supra* note 46. *See also* JAMES MACGREGOR BURNS, LEADERSHIP 4 (Harper & Row 1978) (describing "transforming leaders" as those who engage followers in moral elevation, converting them into leaders themselves).

[996] *See, e.g.,* Mingjun Deng & Hao Tang & Wenbing Luo, *Can the Green Experience of CEOs Improve ESG Performance in Heavy-Polluting Companies? Evidence from China*, 45 MANAGERIAL DECISION ECON. 2373 (2024), https://doi.org/10.1002/mde.4149 (finding that CEOs' prior "green experience" enhances ESG performance through green innovation and reduced financing constraints); Ethan Xin Liu & Shifeng Zhou & Jingda Mi, *Diversity Breeds Strength: CEO Functional Experience Diversity and Corporate ESG Performance*, 34 BUS. STRATEGY & ENVT. 4832 (2025), https://doi.org/10.1002/bse.4227 (demonstrating that greater diversity in CEOs' functional experience boosts ESG performance, especially in manufacturing and non-state-owned enterprises, while board friendship ties and media attention moderate the effect).

[997] For a review of the literature on ESG and executive compensation, *See* Hussainey Al-Shaer & Mahbub Zaman, *CEO Compensation and Sustainability Reporting Assurance: Evidence from the UK*, 158 J. BUS. ETHICS 233 (2019); HOSTETTLER & CO., *Pay-for-Sustainability: How to Reflect ESG in Modern Compensation Systems* (2018), https://www.oebu.ch/admin/data/files/section_asset/file_de/3314/201805_viewpoint_-_esg%5B1%5D.pdf?lm=1540370871; Sean J. Callan & Janet M. Thomas, *Relating CEO Compensation to Social Performance and Financial Performance: Does the Measure of Compensation Matter?,* 21 CORP. SOC. RESP. & ENVTL. MGMT. 202, 205–07, 224–25 (2014); Badawi & Bartlett, *supra* note 59.

[998] *See* Christiane Flammer, Bryan Hong & Dylan Minor, *Corporate Governance and the Rise of Integrating Corporate Social Responsibility in Executive Compensation: Effectiveness and Implications for Firm Outcomes*, 40 STRATEGIC MGMT. J. 1097, 1099 (2019).

culture would not be enough to improve the acquirer's ESG score, as a cultural change of this magnitude would have to come from its top executives.

The culture synergy hypothesis, when applied to ESG culture, suggests different results. A firm that buys a target with a higher ESG culture would benefit from learning from it. Specifically, the acquisition of a sustainable firm could show that the acquirer wants to learn from the target on how to increase social and environmental screening and manage these risks. An acquirer with a lower ESG culture may use the acquisition as a mechanism to elevate its sustainability profile, absorbing target's established ESG culture and leveraging its existing sustainability frameworks. Therefore, the target would transfer knowledge to the acquirer, that, in turn, would use them to break internal inertia, change bad practices and improve its ESG culture. In this scenario, one could expect the ESG culture of the acquirer to increase in the post-merger as a result of a learning expectation.

Similarly, a firm with a strong ESG culture acquiring a weaker ESG target may act as a change agent, instilling sustainability-oriented practices, stakeholder engagement frameworks, and environmental risk management protocols into the newly acquired firm. The extent to which these benefits materialize depends on the acquirer's absorptive capacity and the degree of organizational flexibility in adapting to new cultural dynamics.[999] There is also another possible effect: a company that buys a target with a lower ESG culture could maintain its own ESG performance or even see a spill-over of the target's bad behavior on its culture and a consequent decrease in its ESG score. An empirical study supporting the culture synergy theory, that utilized textual analysis of 10-K forms, reported that greater cultural distance positively affects abnormal short-term stock returns as investors perceive space for culture improvement of the acquirer.[1000]

This research analyzes the acquirer's ESG culture right after the deal announcement and over the following year,[1001] to track transformations of sustainable practices over time. This allows for the identification of any possible greenwashing intent by the acquirer when closing the deal.

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[999] *See* Martiny, *supra* note 108.

[1000] *See* Anne Tremblay, *Cultural Differences, Synergies and Mergers and Acquisitions* (LAVAL UNIV. WORKING PAPER, 2018), https://ssrn.com/abstract=2895110.

[1001] *See infra* Part 4.3.

Greenwashing is a selective disclosure whereby companies publicize positive actions while hiding negative ones to create a misleadingly positive public impression.[1002] This practice reinforces firms' social image to divert the attention of stakeholders from areas of criticism.[1003] Investors, customers, and other stakeholders are putting increasing pressure on companies to disclose exposure to environmental and social risks, as well as to take actions to manage those risks.[1004] However, the greater the disclosure of sustainability data, the greater the opportunities and incentives for companies to greenwash their behavior.[1005] Furthermore, the lack of regulation until recently and the consequent proliferation of different approaches to ESG reporting encourage greenwashing.[1006]

When analyzing the company's ESG culture over the course of a year, it's possible to identify whether the purchase of a target with a better ESG was intended to greenwash or really learn from the target's sustainable practices. Even if it is not the driver of the deal, getting a better ESG score from a "good" target can be something that matters, at least at the margin, because of the opportunity to increase reputation. The gain of reputation is usually associated with ESG adoption.[1007] Therefore, if the firm is able to maintain the higher ESG culture obtained with the M&A, it may mean that it was indeed willing to improve its culture and that it effectively learned from the target. Otherwise, there would be evidence that the firm's objective was only to improve

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[1002] *See* Christopher Marquis, Michael W. Toffel & Yanhua Zhou, Scrutiny, *Norms, and Selective Disclosure: A Global Study of Greenwashing*, 27 **ORG. SCI.** 483 (2016); Thomas P. Lyon & John W. Maxwell, *Greenwash: Corporate Environmental Disclosure Under Threat of Audit*, 20 J. ECON. & MGMT. STRATEGY 3 (2011).

[1003] *See* Mary-Hunter McDonnell & Brayden G. King, *Keeping Up Appearances: Reputational Threat and Impression Management after Social Movement Boycotts*, 58 ADMIN. SCI. Q. 387 (2013) (showing that firms targeted by boycotts often respond with "pro-social claims" to reinforce their social image and dilute stakeholder criticism).

[1004] *See* Matteo Ghitti, Gianfranco Gianfrate & Laura Palma, *The Agency of Greenwashing* (2020) (unpublished manuscript), https://ssrn.com/abstract=3629608, http://dx.doi.org/10.2139/ssrn.3629608.

[1005] *See* William S. Laufer, *Social Accountability and Corporate Greenwashing*, 43 J. BUS. ETHICS 253 (2003); Lyon and Ma Maxwell, *supra* note 185.

[1006] *See* Leo E. Strine, Jr., Kirby Smith & Reilly Steel, *Caremark and ESG, Perfect Together: A Practical Approach to Implementing an Integrated, Efficient, and Effective Caremark and EESG Strategy*, HARV. JOHN M. OLIN CTR. FOR L., ECON., & BUS., DISCUSSION PAPER NO. 1050 (2020), https://www.law.harvard.edu/programs/olin_center/papers/pdf/Strine_1050.pdf.

[1007] *See* Alex Edmans, *Does the Stock Market Fully Value Intangibles? Employee Satisfaction and Equity Prices*, 101 J. FIN. ECON. 621 (2011); Alex Edmans, *The Link Between Job Satisfaction and Firm Value, With Implications for Corporate Social Responsibility*, 26 ACAD. MGMT. PERSP. 1 (2012); Paul W. Roberts & Grahame R. Dowling, *Corporate Reputation and Sustained Superior Financial Performance*, 23 STRATEGIC MGMT. J. 1077 (2002).

its short-term image and reputation before the stakeholders without necessarily changing its culture.

There are only a few studies closely related to this research, and their findings support the culture synergy theory. One study investigated what happened to the ESG culture of companies that acquired higher ESG targets using a sample of 106 deals in the U.S. from 1997 to 2007.[1008] The authors found that the ESG of the acquirer increased on average following the acquisition.[1009] However, this research has three key limitations. First, it does not examine changes in the ESG culture of acquirers that bought lower-ESG targets. Second, the sample size is relatively small, which may limit the generalizability of the findings. Third, the time range is short, potentially constraining the ability to capture long-term ESG cultural transformations. Another important research focused on a sample of 100 deals in Europe between 2003 and 2017, and the authors also found that the ESG performance of the acquirer increased on average following the acquisition.[1010] Although this study covers a longer time range, other limitations persist, such as the small number of deals analyzed.

This paper examines not only the companies that acquired targets with a higher ESG culture but also those that bought targets with a lower ESG culture. This approach offers a much more comprehensive picture of the relationship between M&As and ESG. Moreover, while other studies analyze the ESG culture of the acquirer only right after the deal, this research examines the culture across multiple timeframes, up to one year after the deal announcement, in order to investigate whether the company is able to maintain its new score. To my knowledge, no other research examines a longer impact of M&A on ESG culture. Finally, this research has a larger sample of deals to work with, as the number of companies with ESG scores increased over time.[1011]

[1008] *See* Nihat Aktas, Eric de Bodt & Jean-Gabriel Cousin, *Do Financial Markets Care About SRI? Evidence from Mergers and Acquisitions*, 35 J. BANKING & FIN. 1753 (2011).

[1009] *Id.*

[1010] *See* Tampakoudis & Anagnostopoulou, *supra* note 22.

[1011] *See infra* Part 4 for more information about data used in this research.

3.2. The Role of Abnormal Returns in ESG-M&A Analysis

The second literature this research engages with is the value creation from both the shareholder primacy perspective and the stakeholder governance perspective. In addition to investigating what happens culturally when companies with different ESG cultures enter an M&A deal, this paper examines the financial implications of it in terms of acquirers' cumulative abnormal returns (CAR). Specifically, it investigates *whether an acquisition of a higher or lower ESG target impacts the abnormal returns of the acquirer's stocks over time*. The study of abnormal returns is one of the most common methods used in financial literature to measure the effects of bid announcements.[1012] Empirical studies report positive and statistically significant returns in general for targets right after the announcement of the deal, while the results for acquirers are inconclusive as the returns are either negative or insignificant.[1013]

A benefit of this framework is that it helps to avoid some of the endogeneity problems between ESG performance and financial performance. It is not yet clear whether ESG improves the financial performance of companies or whether firms with better financial performance are the ones that invest the most in ESG practices because they have more resources to do so.[1014] ESG studies have struggled to establish this direction of causation because they usually examine the ESG performance and the financial performance of the same firm. This research relates the ESG performance of the target to the financial performance of the acquirer, which are two different companies, softening endogeneity issues.

The business case for the adoption of ESG practices[1015] is based on the stakeholder theory.[1016] For many of the advocates of this view, sustainable behavior and profit are not mutually

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[1012] *See generally* Gregor Andrade, Mark Mitchell & Erik Stafford, *New Evidence and Perspectives on Mergers*, 15 J. ECON. PERSP. 103, 103–20 (2001); Robert F. Bruner, *Does M&A Pay? A Survey of Evidence for the Decision-Maker*, 12 J. APPL. CORP. FIN. 48, 48–68 (2002); *See* Ruback & Jensen, *supra* note 140.

[1013] *See, e.g.,* Andrade, Mitchell & Stafford, *supra* note 36 (finding that, on average, target firms experience significant positive abnormal returns, while acquirers break even or experience small losses).

[1014] *See* Aktas et al., *supra* note 191; Karen Fisher-Vanden & Karin S. Thorburn**,** *Voluntary Corporate Environmental Initiatives and Shareholder Wealth*, 83 J. ENVTL. ECON. & MGMT. 173 (2008).

[1015] *See supra* Part 2 (discussing how ESG is based on financial perspectives, differently from CSR practices).

[1016] *See* Blair & Stout, *supra* note 2. *See also* Michael E. Porter & Mark R. Kramer, *Creating Shared Value*, in MANAGING SUSTAINABLE BUS. 323, 323–46 (Gilbert G. Lenssen & N. Craig Smith eds., Springer 2019) (arguing that businesses can enhance profitability by addressing social and environmental challenges through the concept of

exclusive, and ESG initiatives enable companies to perform better at least in the long-term. Some think that when business leaders act in the best interest of all stakeholders, they ultimately act in the best interest of the company and its shareholders.[1017] According to empirical studies on the topic, firms that adopt sustainable policies increase their reputation,[1018] reduce their cost of capital,[1019] gain better access to equity financing[1020] and reduce risks,[1021] for example.

Other works report that ESG practices increase corporate performance. A survey of 159 studies found that 63% show a positive relationship between social performance and financial performance, while 15% report a negative relationship and 22% present a neutral or mixed relationship.[1022] In another survey of more than 200 academic articles, 88% of the studies report that sustainable companies have better operational performance, which ultimately translates into cash flows, and 80% of the research say that firms' stock price is positively influenced by sustainability.[1023] Specifically, a research found evidence of the positive relationship between

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creating shared value); ROBERT EDWARD FREEMAN, STRATEGIC MANAGEMENT: A STAKEHOLDER APPROACH (Pitman Publ'g Inc. 1984); Archie Bruce Carroll, *Corporate Social Responsibility: Evolution of a Definitional Construct*, 38 BUS. & SOC'Y 268 (1999); GREGORY JACKSON, *Actors and Institutions*, in THE OXFORD HANDBOOK OF COMPARATIVE INSTITUTIONAL ANALYSIS 63 (Glenn Morgan, John L. Campbell, Colin Crouch, Ove Kaj Pedersen & Richard Whitley eds., Oxford Univ. Press 2010); Daniel T. Ostas, *Postmodern Economic Analysis of Law: Extending the Pragmatic Visions of Richard A. Posner*, 36 AM. BUS. L.J. 193 (2004).

[1017] *See* Porter & Kramer, *supra* note 199.

[1018] *See* Mohamed Arouri, Mathieu Gomes & Kuntara Pukthuanthong, *Corporate Social Responsibility and M&A Uncertainty*, 56 J. CORP. FIN. 176 (2019).

[1019] *See* Rob Bauer & Daniel Hann, *Corporate Environmental Management and Credit Risk*, 59 MGMT. SCI. 236 (2010); Sudheer Chava, *Environmental Externalities and Cost of Capital*, 67 MGMT. SCI. 2223 (2014); Allen Goss & Gordon S. Roberts, *The Impact of Corporate Social Responsibility on the Cost of Bank Loans*, 35 J. BANKING & FIN. 1794 (2011).

[1020] *See* Beiting Cheng, Ioannis Ioannou & George Serafeim, *Corporate Social Responsibility and Access to Finance*, 35 STRATEGIC MGMT. J. 1 (2014); Sadok El Ghoul, Omrane Guedhami, Chuck C.Y. Kwok & Dev R. Mishra, *Does Corporate Social Responsibility Affect the Cost of Capital?*, 35 J. BANKING & FIN. 2388 (2011).

[1021] *See* Arouri et al, *supra* note 201; Pierre Chollet & Blaise W. Sandwidi, *CSR Engagement and Financial Risk: A Virtuous Circle? Evidence from ESG Performance and Credit Ratings*, 47 CORP. GOVERNANCE: INT'L REV. 94 (2018); Olaf Weber, Markus Fenchel & Rainer W. Scholz, *Empirical Analysis of the Integration of Environmental Risks into the Credit Risk Management Process of European Banks*, 35 BUS. STRATEGY & ENV'T 291 (2008); Olaf Weber, Rainer W. Scholz & Gregor Michalik, *Incorporating Sustainability Criteria into Credit Risk Management*, 28 BUS. STRATEGY & ENV'T 48 (2010).

[1022] *See* John Peloza, *The Challenge of Measuring Financial Impacts from Investments in Corporate Social Performance*, 35 J. MGMT. 1518 (2009); GORDON L. CLARK, ANDREAS FEINER & MICHAEL VIEHS, FROM THE STOCKHOLDER TO THE STAKEHOLDER: HOW SUSTAINABILITY CAN DRIVE FINANCIAL OUTPERFORMANCE (Univ. of Oxford & Arabesque Partners 2015).

[1023] *Id.*

employee satisfaction and stock returns,[1024] and another documented that firms experience significant positive stock price reactions when they adopt shareholder-sponsored sustainable proposals.[1025]

In contrast, the traditional shareholder primacy theory considers sustainable activities as additional costs for companies.[1026] Some of these costs are related to agency problems caused by managers who seek to promote their personal interests at the expense of shareholders' wealth.[1027] Friedman famously argued that "there is one and only one social responsibility of business—to use its resources and engage in activities designed to increase its profits so long as it stays within the rules of the game."[1028] Although debated,[1029] this view has been the most prevalent among academics and professionals for decades. It is supported "de jure through case law and de facto through the assignment of votes exclusively to shareholders."[1030] As directors are elected by

[1024] *See* Edmans, *supra* note 190; Alex Edmans, Lucius Li & Chendi Zhang, *Employee Satisfaction, Labor Market Flexibility, and Stock Returns Around the World*, 26 J. FIN. ECON. 159 (2014) (showing international evidence on the positive relationship between employee satisfaction and stock returns).

[1025] *See* Caroline Flammer, *Does Corporate Social Responsibility Lead to Superior Financial Performance? A Regression Discontinuity Approach*, 19 MGMT. SCI. 2549 (2014); Thomas Kaspereit & Kerstin Lopatta, *The Value Relevance of SAM's Corporate Sustainability Ranking and GRI Sustainability Reporting in the European Stock Markets*, 25 BUS. ETHICS: EUR. REV. 1 (2016); Prayag Lal Yadav, Seung Hun Han & Hohyun Kim, *Sustaining Competitive Advantage Through Corporate Environmental Performance*, 26 BUS. STRATEGY & ENVT. 345 (2017); Prayag Lal Yadav, Seung Hun Han & Jae Jeung Rho, *Impact of Environmental Performance on Firm Value for Sustainable Investment: Evidence from Large US Firms*, 25 BUS. STRATEGY & ENVT. 402 (2016).

[1026] *See, e.g.,* Jensen & Meckling, *supra* note 2. *See also* Michael C. Jensen, *Value Maximization, Stakeholder Theory, and the Corporate Objective Function*, 14 J. APPLIED CORP. FIN. 8, 8–21 (2001); HENRY G. MANNE & HENRY C. WALLICH, THE MODERN CORPORATION AND SOCIAL RESPONSIBILITY (1972) (debating the role of corporate social responsibility and its tension with profit maximization, and arguing that shareholder interests should remain the primary concern of corporate managers).

[1027] *See, e.g.,* Jensen & Meckling, *supra* note 2 (arguing that without a clear objective such as shareholder value maximization, managers may use corporate resources to pursue personal agendas, leading to agency costs).

[1028] *See* Milton Friedman, *The Social Responsibility of Business Is to Increase Its Profits*, *N.Y. TIMES MAG.* (Sept. 13, 1970) (articulating the classical economic argument that a corporation's sole social responsibility is to maximize shareholder wealth within the bounds of the law).

[1029] Some scholars argue that directors have always had discretion to observe stakeholders' interest. *See, e.g.,* LYNN A. STOUT, THE SHAREHOLDER VALUE MYTH: HOW PUTTING SHAREHOLDERS FIRST HARMS INVESTORS, CORPORATIONS, AND THE PUBLIC 30–31 (Berrett-Koehler Publishers 2012) (arguing that directors lose their discretion under the business judgment rule "only when a public corporation is about to stop being a public corporation"); **Einer** Elhauge, *Sacrificing Corporate Profits in the Public Interest*, 80 HARV. L. REV. 733, 738, 756–62 (2005) (saying that managers always have "some legal discretion (implicit or explicit) to sacrifice corporate profits in the public interest" and that there is a "fiduciary duty to comply with the law even when compliance requires sacrificing profits.").

[1030] *See* Christopher C. Geczy, Jessica S. Jeffers & David K. Musto, *Institutional Investing When Shareholders Are Not Supreme*, 162 U. PA. L. REV. 75 (2015).

shareholders, they are considered to own fiduciary duties to them. In addition, current governance mechanisms do not incentivize managers to embrace stakeholder view[1031]–for example, executive compensation rules tend to make managers more attentive to share price than anything else.[1032]

According to this theory, ESG culture should have a negative effect on corporate value and performance, a finding that is partially confirmed by some studies. For example, a research examining a panel of socially responsible investing funds over multiple decades found that community relations screening increased financial performance, but environmental and labor relations screening reduced it.[1033] In a meta-analysis of 35 studies examining the performance of socially responsible investing (SRI), authors show that most studies (15) conclude that SRI vehicles perform in the same way as their conventional benchmarks, 6 find underperformance, and 14 exhibit outperformance.[1034] Other authors revealed that voluntary corporate environmental initiatives yield negative stock performance, according to a sample of 58 U.S. firms that joined Climate Leaders, a program related to climate change.[1035]

Based on the two theories above, it is possible to hypothesize what may happen with the stocks of the resulting companies from M&A deals.

Under the stakeholder hypothesis, ESG culture creates value for shareholders and positively impacts reputation, risk, cost of capital, access to financing, and operational and financial performance. Therefore, an acquisition of a target with higher ESG culture may have a positive impact on the acquirer's stock abnormal returns. One possible explanation is the expectation that the acquirer will learn from the target's ESG practices and experiences. Learning from the target's ESG practices will add value to acquiring shareholders only if ESG practices are

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[1031] *See, e.g.,* Edward B. Rock, *Adapting to the New Shareholder-Centric Reality*, 161 U. PA. L. REV. 1907 (2013); Lynn A. Stout, *Killing Conscience: The Unintended Behavioral Consequences of "Pay for Performance"*, 39 J. CORP. L. 525 (2013).

[1032] *See* Badawi & Bartlet, *supra* note 59 (documenting the use of ESG compensation within S&P 500 firms during the 2023 proxy season).

[1033] *See* Michael L. Barnett & Robert M. Salomon, *Beyond Dichotomy: The Curvilinear Relationship Between Social Responsibility and Financial Performance*, 27 STRAT. MGMT. J. 1101 (2006).

[1034] *See* Manuel von Wallis & Christian Klein, *Ethical Requirement and Financial Interest: A Literature Review on Socially Responsible Investing*, 18 Bus. Res. Q. 208 (2015).

[1035] *See* Fisher-Vanden & Thorburn, supra note 197.

investment strategies that increase value. On the other hand, the acquisition of a lower ESG culture target may harm the acquirer's stock returns.

Under the shareholder primacy hypothesis, social and environmental responsibility is usually achieved at the expense of the company's financial performance, which indicates that commitments to ESG are decisions that destroy value for shareholders. In other words, the adoption of ESG practices brings higher costs, negatively affecting the company's competitiveness and profitability.[1036] As a result, the market tends to punish firms that acquire high ESG targets, and one should expect to see a negative relationship between the stock returns of the acquirer and the ESG culture of the target. On the other side, the acquisition of a lower ESG target would not impact or even increase the acquirer's stock returns.

As with the ESG culture, this study examines abnormal stock returns right after the M&A and over the following year. Since ESG investments are likely to increase the intangible assets of companies, it is possible that the value of ESG is not fully incorporated into the stock price around the date of the merger announcement but is reflected in better performance over time.[1037] This is in line with the findings of some authors, who argues that the stock market does not fully value intangibles in the form of employee relations but that firms with high employee satisfaction realize long-term abnormal stock returns.[1038]

Other studies have already investigated the impact of ESG on stock market performance in the context of M&A deals. However, the majority has focused only on the short-term, with the analysis of the acquirers' abnormal return around M&A announcements. For example, when investigating whether financial markets care about responsible investment, a study documented that the acquirer's abnormal returns around the deal announcement are positively associated with targets' social and environmental performance.[1039] This indicates that the better the target is in terms of environmental and social performance, the higher the gain for acquirer shareholders.

[1036] *See* Noël Walley & Bruce Whitehead, *It's Not Easy Being Green*, HARV. BUS. REV., May–June 1994, 46.

[1037] *See* Deng et al., *supra* note 149.

[1038] *See* Edmans, *supra* note 190.

[1039] *See* Aktas et al., *supra* note 191. For other studies that measure the impact of ESG on merger abnormal returns, *See* Krishnamurti et al., *supra* note 150., Yen & Andre, *supra* note 149; Arouri et al., *supra* note 201.

Among the few studies on the long-term effects of the acquisition of ESG-aware targets, one found a positive impact on the acquirer's market value for a sample of European deals one year after the transaction.[1040] Another reported positive long-term stock returns for acquirers after examining U.S. mergers from 1992 to 2007, but their study focuses on how the acquirer's past social performance (not the target's past social performance) affects the wealth of their shareholders.[1041] Differently from past studies, this research examines the impact of the target's ESG culture on the acquirer's stock returns across one year period, drawing a picture of how the financial recognition of ESG practices occurs over time.

4. Data and Methodology

4.1. ESG Data

This research follows the approach commonly used by legal and economic scholars and employs ESG scores as a proxy for ESG culture. These scores are built based on many sources, including the growing amount of ESG-realated information disclosed by companies under investors and other stakeholders' pressure.[1042] Despite growing global regulatory efforts,[1043] much of this reporting remains voluntary. As a result, ESG data is often released in unstructured and inconsistent formats, making comparability across firms and industries difficult.[1044] Additionally,

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[1040] *See* Tampakoudis & Anagnostopoulou, *supra* note 22.

[1041] *See* Deng et al., *supra* note 149, at 30 (arguing that "the results suggest that firms that integrate various stakeholders' interests in their business operation engage in investment activities that enhance their long-term profitability and efficiency, which ultimately increases shareholder wealth and corporate value, supporting the stakeholder value maximization view.")

[1042] *See* JON LUKOMNIK & JAMES P. HAWLEY, MOVING BEYOND MODERN PORTFOLIO THEORY: INVESTING THAT MATTERS (Routledge 2018).

[1043] *See, e.g.,* **EUROPEAN UNION**, Directive (EU) 2022/2464 of the European Parliament and of the Council of 14 December 2022 amending Regulation (EU) No. 537/2014, Directive 2004/109/EC, Directive 2006/43/EC, and Regulation (EU) No. 537/2014, as regards corporate sustainability reporting, 2022 O.J. (L 322) 15; ***The Enhancement and Standardization of Climate-Related Disclosures for Investors***, SECURITIES ACT RELEASE NO. 33-11275, EXCHANGE ACT RELEASE NO. 34-99678, 89 Fed. Reg. 21,668 (Mar. 28, 2024) (to be codified at 17 C.F.R. pts. 229, 232, 239, 240, 249, and 274); **Climate Corporate Data Accountability ACT**, Cal. S.B. 253, 2023–2024 Leg., Reg. Sess. (Cal. 2023); **Climate-Related Financial Risk ACT**, Cal. S.B. 261, 2023–2024 Leg., Reg. Sess. (Cal. 2023).

[1044] *See* Jill E. Fisch, *Making Sustainability Disclosure Sustainable*, 107 **GEO. L.J.** 923 (2019).

companies often do not disclose all aspects of their practices. ESG data may be selectively released to serve strategic objectives, leading to significant variation in the quality and accuracy of reports, which are also rarely subject to independent audit.[1045]

Another reason for this data disorder is that the definition of ESG itself is nebulous. The scope[1046] ranges from environmental topics, such as climate change and water supply, to issues related to workplace relationships, like gender equality and diversity; technology problems, like privacy and cybersecurity; supply chain challenges, such as product source traceability and corruption; among others.[1047] As corporations are continuously facing new challenges with social dimensions, ESG also evolves to embrace them.[1048]

This scenario has led to emergence of ESG rating firms.[1049] These agencies aim to collect, assess, and assign ratings to this data, providing investors, regulators and researchers with insights into a company's sustainability practices.[1050] ESG ratings serve as tools for investors to assess the non-financial dimensions of corporate performance, helping identify firms that demonstrate a commitment to sustainable operations, an attribute that can support long-term value creation.[1051] The ESG landscape is extensive and intricate, encompassing over 600 agencies currently issuing ESG scores.[1052]

[1045] *Id.*

[1046] *See, e.g., Principles for Responsible Inv*. (2018), ANNUAL REPORT 2018, 15-16, https://www.unpri.org/Uploads/g/f/c/priannualreport_605237.pdf (discussing examples of actions on climate change, water, human rights, labor etc.) (last visited Mar. 3, 2025).

[1047] See, e.g., Terry Morehead Dworkin & Cindy A. Schipani, Linking Gender Equity to Environmental Sustainability, 2018 Mich. St. L. Rev. 129 (2018); Antonio G. Valdez & Martha C. Hernandez, Corporate Social Responsibility: A Case Study Approach, 9 Int'l J. Bus. & Soc. Sci. 1 (2016); Kent D. Walker, The Law of Corporate Social Responsibility: The Case of Climate Change Disclosure, 42 Colum. J. Envtl. L. 1 (2018).

[1048] *See* Gadinis & Miazad, *supra* note 60.

[1049] *See, e.g.,* Ajithakumari Vijayappan Nair Biju, Snehith Jacob Kodiyatt, P. P. Nithi Krishna & Geetha Sreelekshmi, *ESG Sentiments and Divergent ESG Scores: Suggesting a Framework for ESG Scoring*, 1 INT'L J. CORP. SOC. RESPONSIBILITY 1 (2023), https://link.springer.com/article/10.1007/s43546-023-00592-4.

[1050] *Id.*

[1051] *See, e.g.,* Brian Tayan, *ESG Ratings: A Compass Without Direction*, HARV. L. SCH. F. ON CORP. GOVERNANCE (Aug. 24, 2022), https://corpgov.law.harvard.edu/2022/08/24/esg-ratings-a-compass-without-direction/ (last visited Mar. 3, 2025).

[1052] *See* Kezia Farnham, *What Are ESG Risk Scores and Why Do They Matter?*, DILIGENT INSIGHTS (Nov. 28, 2023), https://www.diligent.com/resources/blog/esg-risk-scores. For more information on different ratings, *See,*

However, ESG ratings have faced criticism, primarily due to inconsistencies among scores and methodologies.[1053] A study analyzing data from six prominent ESG rating agencies revealed significant discrepancies, attributed to variations in scope, measurement, and weighting of ESG factors.[10547] This divergence can create confusion among investors and undermine the credibility of ESG ratings.[1055]

Moreover, the absence of agreed objectives and regulatory oversight has raised concerns about the reliability of these ratings. To address these issues, the European Union (EU) has initiated steps to regulate ESG rating agencies.[1056] In November 2024, the EU adopted the Regulation on the Transparency and Integrity of ESG Rating Activities, aiming to enhance transparency and consistency in their evaluations.[1057] This regulation requires ESG rating providers operating within the EU to be authorized by the European Securities and Markets Authority (ESMA) and to disclose their methodologies, models, and key rating assumptions.[1058] The regulation seeks to improve the credibility, transparency and comparability of ESG ratings by scrutinizing ratings provider methodologies and vetting providers for potential conflicts of interest.[1059]

Despite these criticisms, some scholars argue that the variation in ESG ratings is not inherently problematic. Similar to traditional equity research reports, which may vary in their buy, sell, or hold recommendations based on distinct methodologies and perspectives, ESG rating discrepancies reflect differing assessments of which intangible factors are most critical to a

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e.g., ESG NAVIGATOR, *ABCs of ESG Ratings Reporting*, https://esgnavigator.com/knowledge-hub/esg-ratings-library/abcs-of-esg-ratings-reporting/.

[1053] *See, e.g.,* Florian Berg, Julian F. Koelbel & Roberto Rigobon, *Aggregate Confusion: The Divergence of ESG Ratings*, 26 REV. FIN. 1315 (2022), https://academic.oup.com/rof/article/26/6/1315/6590670.

[1054] *See* Biju et al., *supra* note 232.

[1055] *Id.*

[1056] *See* COUNCIL OF THE EUR. UNION, *Envtl., Soc. & Gov. Ratings: Council Greenlights New Reg.* (Nov. 19, 2024), https://www.consilium.europa.eu/en/press/press-releases/2024/11/19/environmental-social-and-governance-esg-ratings-council-greenlights-new-regulation/ (last visited Mar. 3, 2025).

[1057] *See* Sebastian J. Barling & Simon Toms, *EU Adopts Legislation to Regulate ESG Rating Providers*, SKADDEN (July 9, 2024), https://www.skadden.com/insights/publications/2024/07/eu-adopts-legislation (last visited Mar. 3, 2025).

[1058] *Id.*

[1059] *See, e.g.,* Mary Foley, *ESG Ratings Get Regulated: Why That's a Good Thing for Businesses*, FORBES (May 22, 2024), https://www.forbes.com (last visited Mar. 3, 2025).

company's long-term value.[1060] This diversity of perspectives is not exactly bad; rather, it can encourage investors to critically assess which ESG factors are most relevant to their investment strategies, fostering a more nuanced understanding of sustainability in the corporate context.[1061]

4.2. The FactSet Truvalue Scores

Following academic researchers in economics and business law,[1062] this project uses ESG scores from FactSet Truvalue Scores & Spotlights, a technology company that employs artificial intelligence to generate ESG metrics.[1063] Initially an independent company, Truvalue was recently acquired by FactSet, a global provider of integrated financial information. Truvalue's differential is that it analyses more than companies' sustainability reports; it applies AI to inspect over 200,000 unstructured text sources in many languages, including news, trade journals, nongovernmental organizations, and industry reports.[1064] Because of the breadth of this data, the use of Truvalue's scores may help to minimize the typical bias of ESG data, which is the fact that the largest and wealthiest companies are generally the most capable of releasing ESG information. Also, firms with greater ESG risks often engage in more proactive ESG disclosures. Thus, metrics based only on companies' disclosure are often biased against firms that release less ESG data because of their financial conditions or because they do not need to manage an ESG risk.

[1060] *See* Alex Edmans, *The End of ESG*, 52 FIN. MGMT. 3, 9 (Spring 2023), https://ssrn.com/abstract=4221990 or http://dx.doi.org/10.2139/ssrn.4221990.

[1061] *Id.*

[1062] See Adam B. Badawi & Frank Partnoy, Measuring the Value of Corporate Governance, 75 Bus. Law. 109 (2020); Alok Kumar Cheema-Fox, Bridget R. LaPerla, George Serafeim & Hui Wang, Corporate Resilience and Response During COVID-19, Harv. Bus. Sch. Acct. & Mgmt. Unit Working Paper No. 20-108 (2020), https://ssrn.com/abstract=3578167; Caterina Consolandi, Robert G. Eccles & Giacomo Gabbi, Sustainability Disclosure and Firm Risk: Evidence from the COVID-19 Pandemic, 68 J. Risk & Fin. Mgmt. 1 (2020).

[1063] *See* FACTSET, FactSet *Truvalue Scores and Spotlights*, https://www.factset.com/marketplace/catalog/product/factset-truvalue-scores-and-spotlights (last visited Mar. 18, 2025).

[1064] *Id.*

Truvalue's ESG categories reflect 26 topics or issues defined by the Sustainability Accounting Standards Board, or SASB,[1065] considered one of the most important models for identifying material sustainability issues.[1066] These topics are part of five sustainability dimensions, also defined by SASB: Environment, Social Capital, Human Capital, Business Model & Innovation, and Leadership & Governance. Covering over 260,000 public and private companies, FactSet Truvalue generates short-term, long-term, and momentum scores. This research focuses on the composite "All Categories," which aggregates firms' scores across all 26 SASB categories to provide a single, overall score.

4.3. Mergers and Acquisitions (M&A) Data

This article uses M&A data from the SDC database, covering the period from 2007, when the Truvalue ESG score database begins, to 2019. It also applies the following sample selection criteria:

- Both the acquirer and target are public firms, as the research needs stock prices available to examine the abnormal return;
- The status of the deal is completed;
- The transaction value is at least $1 million;[1067]
- It excludes transactions labeled as minority stake purchases, acquisitions of remaining interest, spinoffs, recapitalizations, self-tenders, exchange offers, or repurchases;
- Both acquirer and target are rated by Truvalue, with the "All Categories" score, before the announcement of the M&A deal and all timeframes.

[1065] *See* SUSTAINABILITY ACCOUNTING STANDARDS BOARD, *SASB Materiality Map*, SASB, https://www.sasb.org/standards/materiality-map/ (last visited Aug. 13, 2025).

[1066] *See* Badawi & Partnoy, *supra* note 245; Fisch, *supra* note 227.

[1067] *See* Aktas et al., *supra* note 191; Alexandridis et al., *supra* note 166; Tampokoudis et al., *supra* note 22.

- Since the article examines what happens culturally when companies with different ESG cultures enter an M&A deal, the acquirer and target need to have different ESG scores from Truvalue before the deal.

4.4. Methodology and Control Variables

This research explores the rationale behind ESG in the M&A framework through a three-pronged approach: theoretical, empirical, and normative. First, it critically examines the theories of how ESG and M&A can relate to and influence each other. Next, it empirically explores the correlation between ESG culture and M&A transactions by analyzing how deals impact sustainability practices. Finally, it assesses the broader implications of this relationship for policy development, with a particular focus on ESG disclosure requirements under federal securities law. This study is guided by the following research questions: 1. Does the acquisition of a target with higher or lower ESG culture than that of the acquirer in the pre-merger stage affect the ESG culture of the acquirer in the post-merger stage?; 2. Does the acquisition of a target with higher or lower ESG culture than that of the acquirer in the premerger stage affect the stock price abnormal return of the acquirer following the deal?

As most previous papers examining the relationship between ESG and corporate performance, this article employs a prescriptive analysis followed by linear regression and estimations based on the Ordinary Least Squares (OLS) methodology.[1068] To examine the first research question –whether the acquisition of a target with lower or higher ESG culture affects the acquirer's ESG culture–, the research connects the two databases—ESG and M&A— having ESG performance as the dependent variable. ESG performance was analyzed across multiple periods of time within the window from six months prior to the M&A deal to one years after it.[1069]

To answer the second research question, about the acquirer's performance following the acquisition of a target with a different ESG culture, the article investigates stocks' abnormal return in face of two competing theories of ESG: stakeholder and shareholder views. Studies have shown

[1068] *See* Aktas et al., *supra* note 191; Tampokoudis et al., *supra* note 22; Bereskin et al., *supra* note 75.

[1069] *See* more details in *infra* Part 5.

that the abnormal return is sparsely affected by the characteristics of the company and the deal, unlike a firm value variable such as Tobin's Q.[1070] The most accepted method to assess the impact of an event, such as an M&A, on the value of a firm is the event study methodology, which is applied here.[1071] The abnormal returns are the differences between a single stock or portfolio's performance and the expected return over a set period.

To improve the results, this research uses many control variables that may be related to corporate culture and abnormal returns, according to the literature. Some are deal-specific characteristics (same industry, relative size between target and acquirer, deal value, deal year), and others are firm-specific characteristics (profitability, business scale, nation).

Regarding deal characteristics, this paper controls for *same industry* deals, where the acquirer and target are from the same sector (defined based on the Standard Industrial Classification, SIC, System). Previous studies demonstrate that the acquirer's abnormal returns are related to whether the merger was diversified or focused.[1072] Another variable is the *relative size* of the target compared to the acquirer, that is, the relationship between the companies' market value four weeks before the deal. Acquirers are categorized as either slightly larger or much larger than the targets. Abnormal returns tend to be greater when the target and the acquirer are of similar size according to the literature.[1073] Additionally, this research controls for *deal value* and *deal year*. Regarding firm-specific characteristics, one control variable used is *profitability*, measured by the

[1070] *See* John C. Coates, Darius Palia & Ge Wu, *Thirty Years of Evolution in the Roles of Boards and Directors,* 69 J. L. & ECON. 695 (2019).

[1071] *See* Eugene F. Fama, Lawrence Fisher, Michael C. Jensen & Richard Roll, *The Adjustment of Stock Prices to New Information*, 10 INT'L ECON. REV. 1 (1969).

[1072] *See* John G. Matsusaka, *Takeover Bids, Management Opposition, and Shareholder Approval,* 78 J. FIN. ECON. 29 (1993); Robert Comment & Gregg A. Jarrell, *Corporate Focus and Stock Returns*, 37 J. FIN. ECON. 67 (1995); R. Glenn Hubbard & Darius Palia, *A Reexamination of the Conglomerate Merger Wave in the 1960s: An Internal Capital Markets View*, 46 J. FIN. 113 (1999); Klaus Gugler, Dennis C. Mueller & B. Burcin Yurtoglu, *Corporate Governance and the Returns on Investment*, 31 J.L. & ECON. 587 (2003); Salma Uddin & Agyenim Boateng, *An Analysis of Mergers and Acquisitions by UK Firms: Implications for Corporate Governance and Performance*, 17 INT'L J. BUS. PERFORMANCE MGMT. 277 (2009).

[1073] *See* Paul Asquith, Robert F. Brunner & David W. Mullins, Jr., *The Gains to Bidding Firms from Merger*, 11 J. FIN. ECON. 121 (1983); Sara B. Moeller, Frederik P. Schlingemann & René M. Stulz, *Firm Size and the Gains from Acquisitions*, 73 J. FIN. ECON. 201 (2004).

net income over the last 12 months.[1074] Another is *business scale*, measured as net sales over the last 12 months. Finally, the paper controls for *nation*—if the deal has both acquirer and target from the U.S. or if it is a cross-border transaction.

5. Results

5.1. Shifts on ESG Culture Following M&A: Descriptive Analysis

Table 1 presents summary statistics for the ESG scores of acquirers and targets at multiple time points around the M&A deal announcement. It also presents statistics for the relative size ratio of the acquirer to the target and for the ESG scenarios—scenario 1 includes deals in which the acquirer ESG score is higher than the target ESG score, and scenario 2 is the opposite. The descriptive analysis is based on a final sample of 250 M&A transactions with complete ESG and market capitalization data in all the time windows examined.

The average ESG score for acquirers one day before the deal is 52.96, closely matched by their score one month before the deal (52.94), suggesting stability in acquirer ESG positioning prior to the M&A announcement. In contrast, targets show slightly lower average ESG scores than acquirers, 52.62 (1 day before) and 52.69 (1 month before), with greater dispersion (standard deviation of 16.23 compared to 12.38 for acquirers), indicating more heterogeneity among the ESG profile of targets.

Following the deal, the statistics show that acquirers' ESG scores decrease modestly over time. The average ESG score drops to 52.10 one month after, 50.54 six months after, and 50.75 one year after the transaction. This reduction may be attributed to integration problems that usually accompany an M&A deal. The decline is consistent across the median and the mean, with the standard deviation holding somewhat stable, suggesting the decline is widespread rather than driven by a few outliers.

[1074] For studies controlling for different measures of profitability, *See* Bereskin et al., *supra* note 75; Robert G. Eccles, Ioannis Ioannou & George Serafeim, *The Impact of Corporate Sustainability on Organizational Processes and Performance*, 60 MGMT. SCI. 2835 (2014).

In terms of relative firm size, the average size ratio (acquirer market cap ÷ target market cap) is 11.12, with a median of 5.37 and a standard deviation of 14.93, indicating that acquirers are, on average, significantly larger than targets, but the distribution is highly skewed. The minimum ratio in the sample is 0.98, indicating a few deals where the target is larger than the acquirer. Finally, the table presents statistics for both ESG scenarios, based on ESG scores one day before the deal. It shows relatively balanced distribution: 52.8% of deals involved acquirers with higher ESG scores than their targets (Scenario 1), while 47.2% of deals involved acquirers with lower ESG than their targets (Scenario 2). This near-even split enables a meaningful comparison across scenarios in subsequent analyses.

Table 1. Summary Statistics – ESG Scores

Variable	Mean	Median	SD	Min	Max
Acquirer ESG (1 Day Before)	52.96	53.27	12.38	14.90	91.49
Acquirer ESG (1Month Before)	52.94	53.64	12.52	15.01	91.44
Target ESG (1 Day Before)	52.62	52.57	16.23	7.50	99.72
Target ESG (1 Month Before)	52.69	52.85	16.23	7.55	99.68
Acquirer ESG (1 Month After)	52.10	52.75	11.68	17.41	87.73
Acquirer ESG (6 Months After)	50.54	50.55	11.02	19.62	85.88
Acquirer ESG (1 Year After)	50.75	50.42	11.25	23.06	88.74

Variable	Mean	Median	SD	Min	Max
Size Ratio (Acquirer / Target)	11.12	5.37	14.93	0.98	71.44

ESG Scenario Breakdown (based on 1-day-before ESG scores)

Scenario	Definition	Percentage
Scenario 1	Acquirer ESG > Target ESG	52.8%
Scenario 2	Acquirer ESG < Target ESG	47.2%

Notes: 1. ESG scores are from FactSet Truvalue, ranging from 0 to 100, based on AI-driven analysis of public data. 2. “Before” and “After” refer to time around the deal announcement: 1 day and 1 month before, and 1, 6, and 12 months after. 3. Size Ratio = Acquirer Market Capitalization ÷ Target Market Capitalization, using values from 4 weeks prior to announcement. 4. The table includes 250 M&A deals with complete ESG and market value data. 5. Scenario 1 reflects deals where the Acquirer ESG score is higher than the Target's one day before the announcement; Scenario 2 reflects the opposite.

5.2. Shifts on ESG Culture Following M&A: Regression Analysis

To assess whether the acquirer’s ESG culture improves following the acquisition and whether this effect differs depending on the relative ESG performance of the target, this research begins by estimating baseline regressions. It uses two pre-deal ESG baselines: one based on ESG scores 1 day before the deal announcement (Table 2), and another based on scores 1 month before (Table 3). In both models, the dependent variable is the change in the ESG score of the acquirer, which is measured at 1 month, 6 months, and 1 year after the deal announcement.

The main explanatory variable of interest is a binary scenario indicator: Scenario 2 involves deals in which the acquirer’s ESG score was lower than the target’s ESG before the transaction, while Scenario 1 (the reference category) includes deals where the acquirer had a higher ESG score than the target. The control variables applied here include the relative size of the acquirer to the

target, using two dummy variables: “Acquirer Much Larger” and “Acquirer Slightly Larger,” with “Target Larger” as the omitted category.

Table 2 presents the results of this baseline regression. In the model using ESG scores from 1 day before the deal, Scenario 2 shows a positive and statistically significant variation across all three time points. The estimated effect increases over time: firms in Scenario 2 see, on average, a 0.641-point higher ESG score after 1 month ($p < 0.01$), a 3.86-point increase after 6 months ($p < 0.001$), and a 5.80-point improvement after 1 year ($p < 0.001$), relative to Scenario 1. This suggests that when the acquirer has a lower ESG culture than the target, the acquirer tends to benefit from the deal and improve its ESG profile after that.

The results are consistent when using ESG scores from 1 month before the deal (Table 3) as the baseline. The coefficient of Scenario 2 continues positive and statistically significant at all post-deal time points: 0.713 at 1 month ($p < 0.05$), 3.93 at 6 months ($p < 0.001$), and 5.87 at 1 year ($p < 0.001$). These findings reinforce that acquirers tend to improve their ESG culture when they buy targets with higher ESG standards, suggesting a learning effect.

By contrast, Scenario 1 (acquirers started with higher ESG scores than their targets) serve as the reference group in all models. The negative intercepts across time horizons suggest that this group tends to experience ESG score declines after the merger: by approximately 1.47 points at one month, 5.33 points at six months, and 6.22 points at one year, compared to 1 day before the deal. Similar movement is observed when compared to 1 month before the deal. This trend indicates that acquiring a lower ESG target may pose risks to the acquirer’s own ESG trajectory, potentially because of integration problems and consequent dilution of ESG culture.

The size ratio variables show a weaker and more mixed pattern. “Acquirer Much Larger” becomes marginally significant at the 6- and 12-month marks in both models ($p < 0.1$), while “Acquirer Slightly Larger” is only marginally significant at the 1-month horizon in the 1-day baseline model. This may indicate that relative size plays a secondary role in post-deal ESG dynamics, especially when the acquirer is only modestly larger than the target. In other words, if the acquirer is much larger, there’s some evidence of a bigger positive ESG shift, though it's not as strong or consistent as the ESG Scenario effect. When the acquirer is only slightly larger, the effect is smaller and not statistically significant.

To check the validity of the model assumptions, I conducted Breusch-Pagan tests for heteroskedasticity, that produced p-values of 0.29 (1 month), 0.25 (6 months), and 0.48 (1 year), suggesting no evidence of heteroskedasticity. However, as a robustness check, I re-estimated the models using robust standard errors (HC1). The results for Scenario 2 continued statistically significant, confirming that the main findings are not sensitive to potential heteroskedasticity.

Table 2: Baseline Regression on ESG (Compared to1 Day Before)

	1 Month	6 Months	1 Year
Scenario 2 (Acquirer ESG < Target ESG)	0.641**	3.859***	5.795***
	(0.237)	(0.879)	(1.261)
Acquirer Much Larger than Target	0.391	1.635+	2.929+
	(0.273)	(0.975)	(1.514)
Acquirer Slightly Larger than Target	0.588+	1.645	0.928
	(0.301)	(1.135)	(1.652)
Num. Obs.	250	250	250
R2	0.043	0.083	0.095
R2 Adj.	0.032	0.072	0.084
AIC	1024.3	1679.5	1862.9
BIC	1041.9	1697.1	1880.5
Log. Lik.	-507.131	-834.766	-926.462
RMSE	1.84	6.82	9.84
Std. Errors	Custom	Custom	Custom

+ p < 0.1, * p < 0.05, ** p < 0.01, *** p < 0.001

	1 Month	6 Months	1 Year

Robust standard errors in parentheses.

Scenario 1 (Acquirer ESG > Target ESG) is the reference group.

Table 3: Baseline Regression on ESG (Compared to 1 Month Before)

	1 Month	6 Months	1 Year
Scenario 2 (Acquirer ESG < Target ESG)	0.713*	3.931***	5.867***
	(0.336)	(0.924)	(1.294)
Acquirer Much Larger than Target	0.434	1.678+	2.972+
	(0.383)	(1.013)	(1.540)
Acquirer Slightly Larger than Target	0.477	1.534	0.817
	(0.423)	(1.199)	(1.694)
Num. Obs.	250	250	250
R2	0.024	0.078	0.093
R2 Adj.	0.012	0.067	0.082
AIC	1197.2	1705.1	1874.8
BIC	1214.8	1722.7	1892.5
Log. Lik.	-593.594	-847.540	-932.423
RMSE	2.60	7.18	10.08
Std. Errors	Custom	Custom	Custom

	1 Month	6 Months	1 Year

+ p < 0.1, * p < 0.05, ** p < 0.01, *** p < 0.001

Robust standard errors in parentheses.

Scenario 1 (Acquirer ESG > Target ESG) is the reference group

5.3. Shifts on ESG Culture Following M&A: Regression with Control Variables

To deepen the analysis, I estimate full regression models that incorporate key variables related to industry, profitability, business scale, and nation, using ESG scores from both 1 day and 1 month before the deal as baselines. Condensed models (Tables 4 and 5) focus on the variables that have proven to be most important for this dynamic, while the complete results—including additional industry, profitability (measure as net income over the last 12 months), and business scale (measured as net sales over the last 12 months) controls—are provided in Appendix Tables A.1 and A.2.

Across both baselines, Scenario 2 (deals in which the acquirer had a lower ESG score than the target) remains positively and statistically significantly associated with post-deal ESG improvements. Specifically, acquirers in Scenario 2 experience, on average, a 0.613-point increase in ESG scores one month after the deal ($p < 0.05$), a 3.94-point increase after six months ($p < 0.001$), and a 6.02-point improvement one year after the deal ($p < 0.001$), relative to those in Scenario 1, under the 1-day baseline model. Results related to the 1-month baseline are highly consistent, with corresponding coefficients of 0.633 ($p < 0.1$), 3.96 ($p < 0.05$), and 6.01 ($p < 0.01$). These findings suggest that acquiring a higher ESG target contributes to a sustained improvement in the acquirer's ESG profile, even after accounting for deal value, firm size, and deal year.

While the regressions emphasize the effect of Scenario 2 relative to Scenario 1, the baseline category—Scenario 1 acquirers (those with initially higher ESG scores than their targets)—is captured in the intercept, along with all other reference categories (e.g., target larger, cross-border, different industry, baseline industry, average scale and profitability). Although the intercept values

themselves are not directly interpretable as ESG score changes, their statistical significance in some models suggests that even baseline firms may experience shifts in ESG performance following the deal. However, these shifts are generally smaller and less consistent than those observed for Scenario 2 acquirers. These results support the view that acquiring a target with weaker ESG performance may pose risks to the acquirer's ESG trajectory, potentially because of integration challenges, dilution of ESG practices, or reputational spillover effects.

The relative size of the acquirer exhibits a more nuanced role. In the 1-day baseline, acquirers much larger than their targets experience a 3.18-point increase in ESG scores after one year ($p < 0.1$), though the effect is not significant at shorter horizons. Acquirers that are only slightly larger than their targets show smaller, non-significant increases across all windows, with coefficients of 0.575 ($p < 0.1$) at 1 month, 1.969 (not significant) at 6 months, and 1.077 (not significant) at 1 year. Under the 1-month baseline, acquirers much larger than their targets show a significant ESG increase at the 1-month window (1.085, $p < 0.05$), and a marginally significant effect one year after (3.409, $p < 0.1$). In contrast, slightly larger acquirers again exhibit smaller and statistically insignificant effects, with coefficients of 0.397, 1.756, and 0.722 across the three windows. These patterns indicate that while larger acquirers may be better positioned to integrate ESG practices from high-performing targets, the dynamic is less robust than the alignment effect captured by the Scenario variable.

Deal value and deal year variables present mixed patterns. Log Deal Value is not statistically significant in any model, suggesting that the size of the transaction does not drive ESG performance changes. Deal Year, however, shows a negative and significant association at the 1-month and 6-month windows in both tables (e.g., -0.130* and -0.487* in Table A.1), implying decreasing ESG gains in more recent years, possibly due to stricter standards and reduced ESG arbitrage opportunities. Deal year captures potential time effects, such as evolving ESG norms or market conditions and expectations across the years in the sample.

Other control variables (see Appendix A.1 and A.2), including industry group dummies, Same Industry (indicating whether the acquirer and target are in the same industry), and US Group (domestic vs cross-border), are not consistently significant across specifications.

To ensure robustness, all models are estimated with heteroskedasticity-consistent standard errors (HC1). The strong and consistent significance of the Scenario 2 coefficients across both baselines and across time horizons reinforces the conclusion that acquiring a higher ESG is a key driver of the improvement of acquirer's post-merger ESG culture.

Table 4: Condensed Regression ESG Scores – 1-Day Baseline

	ESG Change 1M After	ESG Change 6M After	ESG Change 1Y After
Scenario 2 (Target ESG > Acquirer ESG)	0.613*	3.939***	6.018***
	(0.249)	(0.924)	(1.348)
Acquirer Slightly Larger	0.575+	1.969	1.077
	(0.322)	(1.195)	(1.742)
Acquirer Much Larger	0.550	1.409	2.607
	(0.361)	(1.340)	(1.955)
Log Deal Value	0.093	-0.118	-0.588
	(0.137)	(0.509)	(0.742)
Deal Year	-0.130*	-0.487*	-0.367
	(0.059)	(0.219)	(0.320)
Num.Obs.	239	239	239
R2	0.101	0.146	0.146

+ p < 0.1, * p < 0.05, ** p < 0.01, *** p < 0.001

Condensed model includes variables central to ESG dynamics.

Baseline defined using ESG score 1 month before the deal.

Robust standard errors (HC1) in parentheses.

Table 5: Condensed Regression ESG Scores – 1-Month Baseline

	ESG Change 1M After	ESG Change 6M After	ESG Change 1Y After
Scenario 2 (Target ESG > Acquirer ESG)	0.670*	3.761***	5.650***
	(0.334)	(0.918)	(1.300)
Acquirer Slightly Larger	0.379	1.301	0.557
	(0.410)	(1.126)	(1.595)
Acquirer Much Larger	0.441	1.623	2.919+
	(0.409)	(1.124)	(1.591)
Log Deal Value	0.113	0.276	0.150
	(0.122)	(0.334)	(0.473)
Deal Year	-0.074	-0.387+	-0.282
	(0.074)	(0.202)	(0.287)
Num. Obs.	251	251	251
R2	0.030	0.092	0.095
F	1.497	4.977	5.132
Num. Obs.	239	239	239
R2	0.101	0.146	0.146

+ $p < 0.1$, * $p < 0.05$, ** $p < 0.01$, *** $p < 0.001$

Condensed model includes variables central to ESG dynamics.

Baseline defined using ESG score 1 month before the deal.

Robust standard errors (HC1) in parentheses.

Table 6: Summary of Key Regression Results (1-Year Outcome)

Variable	1-Day Baseline	1-Month Baseline	Significance
Scenario 2 (Target ESG > Acquirer ESG)	5.933	5.933	***
Acquirer Much Larger	3.177	3.177	
Acquirer Slightly Larger	0.590	0.590	+
Log Deal Value	-0.162	-0.162	
Deal Year	-0.388	-0.388	*

5.4. Impact on Abnormal Returns: Descriptive Analysis

Table 7 presents the summary statistics of cumulative abnormal returns (CARs) for acquirers for four time periods after the deal announcement: 1 day, 1 month, 6 months, and 1 year. The numbers are in USD thousands. These are calculated according to the market model, consistent with the event study literature, and convey the performance of acquirer's stocks relative to what would be expected based on general market movements.[1075]

The table shows that the mean is consistently positive across all time horizons, starting at $1,097.83 thousand at 1 day and keeping relatively stable at $1,098.26 thousand after 1 month. It drops slightly to $1,087.79 thousand after 6 months and further to $1,065.78 thousand at the 1-year horizon. The median has a similar movement, with a central tendency near $1.77 million in

[1075] *See* Fama et al., *supra* note 254.

most time windows. The high standard deviations (over $1 million in all cases) reflect significant discrepancies in abnormal returns, confirming how different investors can respond to M&A deals.

The minimum and maximum CARs also show significative dispersion. The most negative CAR observed is -$2.63 million (1-day), while the most positive is over $7 million (1-year). The existence of such extreme values suggests that while some acquirers generate significant value from acquisitions, others can lose a lot. Overall, the summary statistics indicates that M&A is associated with positive average abnormal returns for acquirers, although there is great variation across deals and over time. This variability motivates the need to explore deal and firm-level features, such as ESG scenarios and relative size between acquirer and target, that may influence post-M&A market performance.

Table 7: Summary Statistics of Abnormal Returns by Time Window

Time Window	Mean	Median	SD	Min	Max
1Day	1,097.83	1,771.79	1,074.40	-2,633.34	7,007.76
1Month	1,098.26	1,772.52	1,074.56	-2,633.21	7,008.16
6Months	1,087.79	1,756.37	1,066.17	-2,632.37	7,012.54
1Year	1,065.78	1,721.61	1,047.75	-2,606.90	7,017.67

Note: Table reports summary statistics of cumulative abnormal returns (CARs) for acquirers, measured in USD thousand. Returns are reported over 1 day, 1 month, 6 months, and 1 year after the M&A deal announcement. CARs are computed using the market model. Sample includes 250 M&A deals from 2007 to 2019.

5.5. Impact on Abnormal Returns: Regression with Control Variables

To examine the financial implications of ESG culture in M&A deals, I regress acquirer cumulative abnormal returns (CARs) on ESG scenarios, relative size, and their interaction. Tables 8 and 9 and present the results using ESG baselines from 1 day and 1 month before the deal, respectively. Results are shown across four post-deal time windows: 1 day, 1 month, 6 months, and 1 year.

In both tables, Scenario 2 (where the acquirer buys a target with a higher ESG score) does not demonstrate a statistically significant effect on abnormal returns in any of the time windows. The coefficients are positive, which aligns to the expectation that acquiring a strong ESG target could increase value (stakeholder theory), but the results are consistently not significant. These results suggest that buying a target with superior ESG performance does not, in itself, translate into measurable gains (or losses) in shareholder value. While such transactions may improve the ESG score, as demonstrated in earlier regressions, the financial markets may not immediately reward this type of strategic choice. This is likely due to uncertainty around post-deal integration, credibility of ESG signaling, or the delayed realization of ESG-related synergies.

If ESG scenario variable does not significantly predict abnormal returns, the relative size between acquirer and target plays a more important role. In both the 1-day and 1-month baseline regressions, acquirers that are much larger than their targets consistently experience positive and statistically significant abnormal returns, particularly at longer horizons. For example, in the 1-month baseline model, the coefficient on "Acquirer Much Larger" is 2.27 ($p < 0.05$) at the 6-month window and 3.51 ($p < 0.01$) at the 1-year window. These results indicate that larger acquirers may be better positioned to extract value from the transactions, maybe because of their superior integration ability, stronger bargaining power or higher market credibility. By contrast, smaller or similarly sized acquirers do not show consistent or significant effects, revealing the importance of size, rather than ESG considerations, in driving short- to medium-term financial performance following M&A deals. Importantly, the interaction term between ESG scenario and acquirer size is not significant, indicating that the financial benefits associated with being a larger acquirer do not depend on whether the target has a higher or lower ESG score.

Some of the control variables also show meaningful patterns. Acquirer net income is consistently negative and statistically significant across models (e.g., –0.245* in the 1-month baseline), suggesting that more profitable acquirers tend to experience lower abnormal returns following an M&A deal. This somewhat counter-intuitive result may reflect investor concerns that profitable firms are overpaying for targets or engaging in deals that dilute existing high margins, view that has already been noted by the literature.[1076] Other control variable, net sales (used as a

[1076] *See supra* Part 2.

proxy for firm scale), is not significantly associated with abnormal returns, indicating that overall scale alone does not drive market reaction.

In turn, cross-border (international) deals are associated with significantly lower CARs, particularly in the shorter windows. For instance, the coefficient for the cross-border deals variable is –545.87 in the 1-month baseline*, highlighting potential investor skepticism about the risks and complexities of cross-border integration. Meanwhile, deals between firms in the same industry show modestly positive and often marginally significant effects on CARs, suggesting that industry familiarity and synergies may be valued by the market, even if not uniformly in all time windows analyzed.

Table 8: Regression Results – Abnormal Returns vs ESG Scenario and Relative Size (Baseline: 1 Day Before)

	1 Day After	1 Month After	6 Months After	1 Year After
Scenario2: Target ESG > Acquirer ESG	159.763	159.752	156.397	156.405
	(155.366)	(155.355)	(154.156)	(151.625)
Relative Size (Acquirer/Target)	75.534***	75.570***	74.874***	73.487***
	(6.921)	(6.921)	(6.868)	(6.755)
Interaction: ESG Scenario × Size	76.171***	-76.211***	-75.440***	-74.094***
	(9.186)	(9.186)	(9.115)	(8.965)
Deal Value (USD M)	0.017	0.017	0.016	0.016
	(0.011)	(0.011)	(0.011)	(0.011)

	1 Day After	1 Month After	6 Months After	1 Year After
Net Income (USD M)	-0.245***	-0.245***	-0.242***	-0.238***
	(0.050)	(0.050)	(0.049)	(0.049)
Net Sales (USD M)	-0.001	-0.001	-0.001	-0.001
	(0.003)	(0.003)	(0.003)	(0.003)
Same Industry	280.027+	280.269+	281.843*	279.956*
	(144.145)	(144.135)	(143.022)	(140.674)
Cross-Border Deal	-545.866*	545.867*	-542.484*	-536.193*
	(272.569)	(272.549)	(270.445)	(266.005)
F	41.701	41.741	41.726	41.563

* p < 0.1, ** p < 0.05, *** p < 0.01

Baseline defined using ESG score 1 day before the deal.

US Group reference category is fully U.S.-domestic deals. Coefficient indicates difference for cross-border transactions.

Robust standard errors (HC1) in parentheses.

Table 9: Regression Results – Abnormal Returns vs ESG Scenario and Relative Size (Baseline: 1 Month Before)

	1 Day After	1 Month After	6 Months After	1 Year After
Scenario 2: Target ESG > Acquirer ESG	159.763	159.752	156.397	156.405

	1 Day After	1 Month After	6 Months After	1 Year After
	(155.366)	(155.355)	(154.156)	(151.625)
Relative Size (Acquirer/Target)	75.534***	75.570***	74.874***	73.487***
	(6.921)	(6.921)	(6.868)	(6.755)
Interaction: ESG Scenario × Size	76.171***	-76.211***	-75.440***	-74.094***
	(9.186)	(9.186)	(9.115)	(8.965)
Deal Value (USD M)	0.017	0.017	0.016	0.016
	(0.011)	(0.011)	(0.011)	(0.011)
Net Income (USD M)	-0.245***	-0.245***	-0.242***	-0.238***
	(0.050)	(0.050)	(0.049)	(0.049)
Net Sales (USD M)	-0.001	-0.001	-0.001	-0.001
	(0.003)	(0.003)	(0.003)	(0.003)
Same Industry	280.027+	280.269+	281.843*	279.956*
	(144.145)	(144.135)	(143.022)	(140.674)
Cross-Border Deal	-545.866*	-545.867*	-542.484*	-536.193*
	(272.569)	(272.549)	(270.445)	(266.005)
F	41.701	41.741	41.726	41.563

* p < 0.1, ** p < 0.05, *** p < 0.01

Baseline defined using ESG score 1 month before the deal.

	1 Day After	1 Month After	6 Months After	1 Year After

US Group reference category is fully U.S.-domestic deals. Coefficient indicates difference for cross-border transactions.

Robust standard errors (HC1) in parentheses.

6. Discussion and Implications

This study advances the understanding of ESG culture in the context of mergers and acquisitions by bringing three key insights. First, the findings offer novel evidence that M&A transactions can act as a driver of corporate culture change, particularly with respect to ESG values. While prior literature across various disciplines—including psychology, sociology, management, economics, and law—has emphasized the role of corporate culture in shaping business outcomes, fewer studies have focused on what triggers cultural transformation itself. In the M&A literature, most attention has been placed on how cultural compatibility affects integration success, rather than how M&A can reshape corporate culture. This paper helps fill this gap by showing a bidirectional relationship: not only does culture influence the outcome of a merger, as previous studies have proven, but M&A activity itself can induce cultural shifts within the acquiring firm, particularly in terms of ESG practices.

Second, the findings support the culture synergy theory, which posits that acquirers can absorb knowledge and practices from their targets. In this context, deals where the acquirer initially had a lower ESG score than the target (Scenario 2) led to significant and sustained improvements in the acquirer's ESG performance. The improvement was not just right after the deal announcement, what could be sign of a "greenwashing" effect. Rather, the improvement is consistent and even incremental over time, suggesting a genuine internalization of ESG values. This challenges the concern that firms may engage in ESG-driven acquisitions primarily for reputational purposes without meaningful follow-though commitment.

Overall, these results imply that M&A can offer a pathway for firms to overcome internal inertia or barriers to ESG adoption by importing a sustainability culture from a more advanced target. They also highlight the importance of including cultural due diligence, not just financial or

operational due diligence, in the pre-deal evaluation process, given the impact that M&A can have on ESG culture. Furthermore, the analysis suggests that relative size between acquirer and target matters. Although not always statistically significant across the time windows analyzed, the data indicate that much larger acquirers are more likely to benefit from the target's ESG culture, potentially because they have greater resources (capital, personnel, managerial capacity) to integrate and institutionalize sustainability practices acquired through the deal.

Third, the findings of this paper talk to the literature of ESG value creation. The economic evidence of post-M&A announcement abnormal returns provides insights into whether markets reward or punish acquirers in terms of making ESG-driven acquisitions. While acquiring a high ESG target is positively associated with ESG score improvements for the acquirer, there is no statistically significant evidence that such transactions are rewarded by investors in the form of abnormal stock returns, even up to one year after the deal. Although the coefficients on abnormal returns are directionally positive across all time windows—which aligns with the stakeholder value creation theory—, the lack of statistical significance suggests that investors may view ESG-driven deals as potentially valuable, but remain cautious in assigning immediate financial value to them. This may reflect uncertainty about the credibility of ESG signaling, or the long-time horizon typically required for ESG-related synergies to materialize, an interpretation consistent with prior literature.[1077]

Importantly, the performance of abnormal returns appears more strongly correlated with the relative size between acquirer and target. Acquirers that are much larger than their targets tend to earn higher CARs, potentially reflecting superior integration capacity, bargaining power, or investor confidence in the acquirer's ability to capture value. This highlights that size, rather than ESG considerations per se, may be the more decisive factor in driving short and medium-term financial outcomes in M&A transactions.

While this paper does not find statistically significant evidence that ESG-driven M&A creates immediate shareholder value, it also does not support the shareholder primacy view that ESG commitments impose a clear financial cost. The generally positive, although insignificant, direction of market reactions suggests a more nuanced reality—one where ESG-related value

[1077] *See* Edmans, *supra* note 190.

creation may be contingent on other factors like execution capacity, strategic alignment, and investor trust in the acquirer's long-term sustainability vision.

6.1. Contributions for Theory and Practice

There are mainly two theoretical contributions of this research. First, it advances the growing literature on the catalysts of corporate culture change, particularly of ESG culture, by demonstrating how a major strategic event such as a merger or acquisition can drive cultural transformation. Previous studies have examined cultural drivers such as managers characteristics,[1078] firms communication styles,[1079] company size and public listing status,[1080] and institutional factors like national context,[1081] but they have largely overlooked how disruptive organizational events affect ESG culture. This study addresses this gap by showing that M&A deals can meaningfully change a firm's ESG trajectory and, therefore, they represent an important—and underexplored—mechanism for sustainability-oriented transformation. Importantly, even if ESG improvement is not the primary motivation behind an M&A deal, the results suggest that acquiring a high ESG target can yield strong and lasting changes in the acquirer's ESG culture.

[1078] *See*, e,.g, Arizkuren-Eleta, A., Gartzia, L., Baniandrés Avendaño, J., del Castillo Mory, E. & Martínez-Lozares, A., *The Influence of Managers and Organisational Profiles in CSR Decision-Making: Ideas for Implementation in the Maritime Sector*, 10 J. MAR. RES. 43 (2013).

[1079] *See, e.g.,* Giulia Miotto & Jan Rom, *CSR in Business Schools: A Theoretical Framework*, 16 BUS. & SOC. 577 (2017).

[1080] *See* Andreas Rasche, Wencke Gwozdz, Mads Lund Larsen & Jeremy Moon, *Which Firms Leave Multi-Stakeholder Initiatives? An Analysis of Delistings from the United Nations Global Compact*, REG. & GOVERNANCE (forthcoming 2020).

[1081] *See, e.g.,* Dirk Matten & Jeremy Moon, *"Implicit" and "Explicit" CSR: A Conceptual Framework for a Comparative Understanding of Corporate Social Responsibility*, 33 ACAD. MGMT. REV. 404 (2008).

Second, this study adds a new dimension to the rich literature on M&A motivations.[1082] It is already well established that strategic synergies,[1083] growth in size,[1084] diversification,[1085] financial synergies,[1086] macroeconomic and institutional conditions[1087] are among the reasons why companies seek a deal. This paper proposes that ESG improvement should be added to that list: changes in sustainability performance can be both a consequence and a potential strategic driver of M&A activity. Future research should therefore consider ESG improvement as an explicit objective or byproduct of mergers, particularly considering evolving stakeholder expectations and regulatory frameworks.

In addition to the theoretical contributions, this study offers significant practical implications for corporate managers, investors, stakeholders, and policymakers. For managers, the results highlight the importance of strategic planning and a forward-looking vision when acquiring a company with a distinct ESG culture. Companies seeking to advance sustainability through M&A need to establish governance structures that support the adoption and integration of ESG practices. Without such structures, potential ESG synergies may be diluted or lost over time. Effective ESG integration post-merger may depend not only on intent, but also on organizational design and leadership commitment.

For investors with ESG priorities, the findings suggest that acquiring high-ESG targets can enhance the acquirer's ESG profile. Accordingly, ESG due diligence should go beyond superficial disclosures to evaluate the depth of the target's commitments and the extent to which sustainability is embedded in its governance systems, risk management processes, and incentive structures.

[1082] *See, e.g.,* Norbert Steigenberger, *The Challenge of Integration: A Review of the M&A Integration Literature*, 19 INT'L J. MGMT. REV. 408 (2017).

[1083] *See, e.g.,* Ziva Rozen-Bakher, *The Trade-Off Between Synergy Success and Efficiency Gains in M&A Strategy*, 13 EUROMED J. BUS. 163 (2018).

[1084] *See, e.g.,* Shaun Owen & Alfred Yawson, *Corporate Life Cycle and M&A Activity*, 34 J. BANKING & FIN. 427 (2010).

[1085] *See, e.g.,* Mehmet E. Akbulut & John G. Matsusaka, *Fifty Plus Years of Diversification Announcements,* 45 FIN. REV. 231 (2010).

[1086] *See, e.g.,* Hayne E. Leland, *Financial Synergies and the Optimal Scope of the Firm: Implications for Mergers, Spinoffs, and Structured Finance*, 62 J. FIN. 765 (2007).

[1087] *See, e.g.,* Kira Lee, *Cross-Border Mergers and Acquisitions Amid Political Uncertainty: A Bargaining Perspective*, 39 STRATEGIC MGMT. J. 2992 (2018).

However, investors must calibrate expectations for short and mid-term financial value from such deals, since the study found no statistically significant relationship with abnormal returns in the first year after acquisition, suggesting that value capture, if at all, could be a longer time horizon.

For regulators, the findings reaffirm the importance of improving the quality and consistency of ESG-related disclosures. Since ESG culture is shown to be transferable among firms within the context of M&A transactions, it is essential that stakeholders, including managers and investors, have a clear and accurate picture of a target's ESG practices. The boundaries of voluntary reporting and the omnipresent risk of greenwashing suggest an increased need for better regulatory frameworks. Therefore, policymakers should consider expanding disclosure obligations, ensuring that sustainability narratives are followed by material commitments and measurable outcomes.

6.2. Limitations and Future Research

Although this study provides some helpful insights into how M&A deals impact ESG culture and abnormal returns, there are several limitations that should be mentioned. In the first place, the study relies primarily on quantitative ESG scores and abnormal returns. While ESG scores represent a useful proxy for sustainability performance—and the source used in this study combines third-party data and AI-driven analysis to reduce the bias of self-disclosures—they may still fail to incorporate the richness of cultural dimensions or the degree of ESG commitments.[1088] Second, this research focuses on short and medium-term post-merger effects, tracking ESG outcomes and market responses up to one year after the deal announcement. However, cultural and organizational change, particularly in the ESG arena, may take more time to materialize. As such, longer-term developments are not fully reflected in the findings and remain a subject for future research. It is worth noting, though, that inconsistent ESG scores over extended periods present an obstacle to this type of analysis.

Moreover, although key firms and deal controls are included, the models probably do not capture all potential relevant contextual factors. Regulatory environments, activist investor

[1088] *See supra* Part 5.

pressure, media scrutiny, and internal governance dynamics (e.g., board composition, executive turnover) could also affect ESG performance post-merger, but were outside the scope of this investigation. Finally, this study is correlational. Although it uses robust controls and modeling, it cannot fully eliminate concerns about selection effects and omitted variable bias. For example, it is possible that acquirers already inclined toward ESG improvements are simply more likely to target firms with strong ESG performance, rather than being transformed by the acquisition itself.

Building on this study, there are several important paths for future research. One possibility is to explore causal mechanisms, despite the challenges it can bring. Future research should employ quasi-experimental methods, such as instrumental variables, difference-in-differences, or matched-sample designs, to better isolate the causal effect of acquiring a high ESG target on the acquirer's ESG trajectory. Another possibility is to investigate the dynamics of cultural integration in greater depth. To understand how ESG values are transferred or curbed after an M&A deal, researchers should pursue qualitative approaches, such as case studies or executive interviews, to examine leadership choices, governance alignment, and resistance to change. More specifically, it would be interesting to better understand by which types of mechanisms the ESG culture is transmitted from target to acquirer. It may be a top-down influence, as leaders decide to buy a higher target, or a bottom-down impact, if the ESG practices are learned first from the ground, arriving later to the leadership.[1089] Another possibility is that learning arises from interactions among diverse actors across different parts of the organization and their engagement with external stakeholders, reflecting characteristics of the mutual constitution theory.[1090]

Future research can also study the influence of external stakeholders. For example, it would be interesting to examine how regulators, NGOs, activist investors, and ratings agencies shape

[1089] For understanding the "bottom-up" theory, *See, e.g.,* DEBRA E. MEYERSON, TEMPERED RADICALS: HOW PEOPLE USE DIFFERENCE TO INSPIRE CHANGE AT WORK (Harv. Bus. Sch. Press 2001) (arguing that cultural change often originates with individuals or small groups inside organizations who, without formal authority, leverage everyday actions to shift norms and values from the ground up); GARY HAMEL, THE FUTURE OF MANAGEMENT (Harvard Bus. Sch. Press 2007) (contending that lasting innovation and cultural transformation require dismantling hierarchical barriers so that ideas and initiatives can emerge organically from employees at all levels).

[1090] *See, e.g.,* Michael L. Tushman & Philip Anderson, *The Mutual Constitution of Persons and Organizations: A Social Network Approach*, 8 ORG. SCI.1, 22 (1997), https://pubsonline.informs.org/doi/10.1287/orsc.2013.0887.

ESG behavior after a merger or acquisition. These actors may apply pressure or provide incentives that influence how acquirers manage inherited ESG practices. Disaggregating ESG dimensions is another possibility. Research can explore if one of the ESG pillars (environmental, social, or governance) is more or less likely to be transferred, retained, or rewarded following an M&A deal. Responses by investors can also vary depending on what dimension is emphasized, yielding more nuanced evidence on stakeholder preferences. This study does, however, have to work with homogeneous data across all three pillars, which may not always be available.

7. Conclusion

This study contributes to the growing literature on ESG by examining how sustainability practices can evolve within firms following major corporate events. While much of the existing research has explored how ESG performance affects firm valuation, investor decisions, or regulatory strategy, this paper shifts the focus to a more understudied question: whether ESG culture itself can change—and under what conditions. Using mergers and acquisitions as a testing ground, the study provides novel evidence that ESG culture is not fixed, but responsive to external organizational shocks.

The findings show that acquirers who purchase firms with stronger ESG profiles tend to experience sustained improvements in their own ESG performance. These results support the idea that ESG values can be transferred and institutionalized through integration, highlighting the role of organizational learning, strategic adoption, or reputational convergence. Importantly, however, this cultural shift is not immediately rewarded by the market. Although abnormal returns are directionally positive, they are not statistically significant, suggesting that investors may be cautious in assigning value to ESG-enhancing transactions in the short and mid-term, up to one year after the deal.

At a time when ESG faces both regulatory momentum and political backlash, these insights are of broader relevance. They caution firms against treating ESG as merely symbolic or reputational, particularly in the face of important strategic moves like mergers and acquisitions.

They also show the need for transparency and accuracy in ESG disclosures, so that stakeholders can assess not only performance metrics, but the likely cultural consequences of M&A activity.

By centering ESG culture—not merely as a reputational signal or compliance metric, but as a dynamic organizational attribute—this study broadens the understanding of what drives sustainability performance over time. It encourages scholars and practitioners to look beyond static ESG ratings and to consider how internal and external forces, including corporate combinations, can reshape the trajectory of a firm's sustainability commitments. As ESG, sometimes rebranded in response to political backlash, continues to have relevance in both public policy and investment strategy, understanding how and when these values take root within companies should be a research priority.

8. Appendix

8.1. Full Regression Output Tables

Appendix Table A.1: Full Regression Model – 1 Day Baseline

	ESG Change 1M After	ESG Change 6M After	ESG Change 1Y After
Scenario 2 (Acquirer ESG < Target ESG)	0.613*	3.939***	6.018***
	(0.249)	(0.924)	(1.348)
Acquirer Much Larger than Target	0.550	1.409	2.607

Appendix Table A.1: Full Regression Model – 1 Day Baseline

	ESG Change 1M After	ESG Change 6M After	ESG Change 1Y After
	(0.361)	(1.340)	(1.955)
Acquirer Slightly Larger than Target	0.575+	1.969	1.077
	(0.322)	(1.195)	(1.742)
Log Deal Value	0.093	-0.118	-0.588
	(0.137)	(0.509)	(0.742)
US Group	0.367	1.443	-0.986
	(0.433)	(1.610)	(2.349)
Same Industry	0.404	0.354	2.023
	(0.319)	(1.185)	(1.728)
Deal Year	-0.130*	-0.487*	-0.367
	(0.059)	(0.219)	(0.320)
Acquirer Industry Finance, Insurance & Real Estate	0.659	3.637	6.321
	(0.892)	(3.313)	(4.832)
Acquirer Industry Manufacturing	0.529	3.903	6.023
	(0.873)	(3.244)	(4.732)

Appendix Table A.1: Full Regression Model – 1 Day Baseline

	ESG Change 1M After	ESG Change 6M After	ESG Change 1Y After
Acquirer Industry Mining	0.673	3.148	7.515
	(1.088)	(4.041)	(5.894)
Acquirer Industry Retail Trade	0.184	3.615	4.994
	(1.299)	(4.828)	(7.042)
Acquirer Industry Services	0.833	3.713	8.815+
	(0.911)	(3.386)	(4.939)
Acquirer Industry Transportation & Utilities	1.117	3.258	5.707
	(0.973)	(3.616)	(5.275)
Acquirer Industry Wholesale Trade	0.145	-0.979	-0.622
	(1.209)	(4.491)	(6.550)
Scaled Acquirer Profitability	-0.008	0.142	-0.296
	(0.155)	(0.575)	(0.838)
Scaled Target Profitability	0.077	0.499	0.728
	(0.131)	(0.487)	(0.711)
Log Acquirer Scale (Net Sales)	0.016	0.439	0.582
	(0.135)	(0.500)	(0.729)
Log Target Scale (Net Sales)	0.018	-0.165	0.074

Appendix Table A.1: Full Regression Model – 1 Day Baseline

	ESG Change 1M After	ESG Change 6M After	ESG Change 1Y After
	(0.119)	(0.440)	(0.642)
Num. Obs.	239	239	239
R2	0.101	0.146	0.146

+ p < 0.1, * p < 0.05, ** p < 0.01, *** p < 0.001

Full model includes industry, financial, and structural controls.

Baseline defined using ESG score 1 day before the deal.

Robust standard errors (HC1) in parentheses.

Appendix Table A.2: Full Regression Model – 1-Month Baseline

	ESG Change 1M After	ESG Change 6M After	ESG Change 1Y After
Scenario 2 (Acquirer ESG < Target ESG)	0.633+	3.960***	6.011***

Appendix Table A.2: Full Regression Model – 1-Month Baseline

	ESG Change 1M After	ESG Change 6M After	ESG Change 1Y After
	(0.342)	(0.969)	(1.384)
Acquirer Much Larger than Target	1.085*	2.003	3.409+
	(0.489)	(1.384)	(1.978)
Acquirer Slightly Larger than Target	0.397	1.756	0.722
	(0.439)	(1.244)	(1.777)
Log Deal Value	0.300	0.123	-0.242
	(0.186)	(0.526)	(0.752)
US Group	0.536	1.622	-0.719
	(0.596)	(1.688)	(2.412)
Same Industry	0.284	0.223	1.844
	(0.438)	(1.241)	(1.773)
Deal Year	-0.114	-0.472*	-0.363
	(0.081)	(0.230)	(0.329)
Acquire Industry Finance, Insurance & Real Estate	0.072	2.979	5.478
	(1.225)	(3.468)	(4.955)
Acquirer Industry Manufacturing	-0.360	2.980	4.980

Appendix Table A.2: Full Regression Model – 1-Month Baseline

	ESG Change 1M After	ESG Change 6M After	ESG Change 1Y After
	(1.201)	(3.400)	(4.857)
Acquirer Industry Mining	-1.124	1.318	5.588
	(1.495)	(4.234)	(6.050)
Acquirer Industry Retail Trade	-0.634	2.815	4.197
	(1.786)	(5.059)	(7.228)
Acquirer Industry Services	0.292	3.134	8.127
	(1.253)	(3.547)	(5.068)
Acquirer Industry Transportation & Utilities	0.694	2.820	5.208
	(1.338)	(3.790)	(5.415)
Acquirer Industry Wholesale Trade	-0.074	-1.183	-0.819
	(1.662)	(4.707)	(6.725)
Scaled Acquirer Profitability	-0.116	0.045	-0.356
	(0.212)	(0.602)	(0.859)
Scaled Target Profitability	0.283	0.710	0.946
	(0.180)	(0.510)	(0.729)
Log Acquirer Scale (Net Sales)	-0.158	0.210	0.165
	(0.172)	(0.487)	(0.696)

Appendix Table A.2: Full Regression Model – 1-Month Baseline

	ESG Change 1M After	ESG Change 6M After	ESG Change 1Y After
Log Target Scale (Net Sales)	-0.019	-0.196	0.098
	(0.157)	(0.445)	(0.636)
Num. Obs.	239	239	239
R2	0.084	0.135	0.140
F	1.127	1.908	1.993

+ p < 0.1, * p < 0.05, ** p < 0.01, *** p < 0.001

Full model includes industry, financial, and structural controls.

Baseline defined using ESG score 1 month before the deal.

Robust standard errors (HC1) in parentheses.

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