

# THE EVOLUTION OF SUSTAINABLE DEVELOPMENT AS A MODERATOR OF CORPORATE GOVERNANCE PRACTICES – THE CASE OF CROATIA

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## ABSTRACT

*As the global business context changes over time, corporate governance practices evolve. Especially through sustainability reporting of organizations the progress and implementation of sustainable development goals linked to the EU, national, and sectoral achievements can be monitored. The purpose of this paper is to determine the level of implementation of sustainable development goals in Croatia and to link national progress with the improvement of corporate governance practices in the segment of corporate sustainability reporting. Using the word cloud method on a sample of 100 largest Croatian companies, the level of transparency in organizational sustainability reporting will be investigated, measured by the application of the provisions of the revised CSRD (Corporate Sustainability Reporting Directive) and the preparations for the challenges posed by the CSDDD (Corporate Sustainability Due Diligence Directive). The research results show that the evolution of sustainable development, measured by the level of national implementation of sustainable development goals, has influenced the evolution of corporate governance practices in Croatia by incorporating social and environmental goals into the creation of added value for organizations. By highlighting the changes in the communication on corporate governance practices, the paper contributes to understanding of the interconnection between sustainable development and corporate governance, and consequently, to the development of improved and more sustainable corporate governance practices in Croatia.*

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**Key words:** *corporate governance practice, Croatian sustainable development achievement, Croatian sustainability-governance word cloud, sustainability reporting.*

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## 1. INTRODUCTION

As the lyrics of the popular last century mid-eighties song performed by Paul Young echo: “Everything Must Change”<sup>1</sup>, the mindset setup for the everlasting change is the most required capability in the contemporary business environment. Nowadays, the lyrics of the song if embedded in the corporate governance research and practice, seem like a prophecy. Corporate governance field and practice are changing fundamentally, ever since the Business Roundtable redefined the purpose of a corporation to promote “An Economy That Serves All Americans”<sup>2</sup> and the Davos Manifesto 2020 declared “The Universal Purpose of a Company in the Fourth Industrial Revolution”.<sup>3</sup> Although companies have their own purpose, the jointly accepted overall purpose of each company is: “to engage all its stakeholders in shared and sustained value creation. In creating such value, a company serves not only its shareholders, but all its stakeholders – employees, customers, suppliers, local communities and society at large”.<sup>4</sup> What a turnaround from the profit-oriented approach towards the wealth and value creation approach in less than one decade. There is no doubt that companies are to operate profitably, but the way they are operating and the footprint they are imprinting is quite different from the early paradigm of profitability without responsibility. Nowadays, the kind of convergence in the corporate governance practice is occurring due to the renewed standards set through the OECD Principles of Corporate Governance in 2023<sup>5</sup>, since they are often incorporated into national laws and regulations. The same scenario is currently going on in Croatia: the companies’ governance practice is changing for it is sustained by the regulatory institutional introduction of the new CSRD requirements. Therefore, we were curious how Croatian companies are responding to the new regulatory framework demands. The findings show that

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<sup>1</sup> Young, P.: *Everything must change*, 1985.

<sup>2</sup> For more details on this matter see Business Roundtable: *Business Roundtable Redefines the Purpose of a Corporation to Promote ‘An Economy That Serves All Americans’*, 19.08.2019.

<sup>3</sup> For more details on this matter see World Economic Forum: <https://www.weforum.org/stories/2019/12/davos-manifesto-2020-the-universal-purpose-of-a-company-in-the-fourth-industrial-revolution/>

<sup>4</sup> World Economic Forum: *Davos Manifesto: The Universal Purpose of a Company in the Fourth Industrial Revolution*, 02.12.2019.

<sup>5</sup> OECD: *G20/OECD Principles of corporate governance*, Paris: OECD Publishing, 2023.

they are moderately adjusting, but the magnitude and pace of response could be evaluated as going slow. The process has its impediments, which is understandable, due to a high level of adjustment requirements of the new regulatory framework.

So, the challenge of this research is to analyse the state of transparency in companies' sustainability reporting in Croatian companies, measured by the application of the provisions of CSRD. In addition, the research is aimed at shedding light on the level of national implementation of sustainable development goals, and its influence on the evolution of corporate governance practices in Croatia, in particular the incorporation of the social and environmental goals into companies' activities and performance. By highlighting the changes in the communication on corporate governance practices, the paper aims to contribute to the understanding of the interconnection between sustainable development and corporate governance, and consequently, to the moderation of more sustainable corporate governance practices in Croatia. The following sections two and three outline the ongoing changes in corporate governance practice and sustainable development initiatives and goals. Chapter four focuses on shaping the national Word Cloud for the sustainable corporate governance practice and explains the research methodology and sample. Chapter five brings the main empirical findings and in further discussion elaborates the most challenging issues for Croatian companies, while the final chapter presents concluding considerations as well as implications for the sustainable corporate governance practice and highlights some potential directions for the future research.

## **2. THE (R)EVOLUTION AND ONGOING GOVERNANCE CHANGES**

Corporate governance as a discipline is facing its paradigmatic transformation. Just as the practice has embraced the shift of the domain's dominant focus, from its traditional agency roots and complete contracting towards an integrated, multi-theoretical, and stakeholder-centric governance perspective<sup>6</sup>, the new requirements are already on the way. In today's rapidly evolving business landscape, corporate governance has transcended from being a static-structured dashboard to becoming a critical framework that shapes the destinies and long-term success of companies and their stakeholders. There is a tangible sense of urgency surrounding governance issues, driven by seismic shifts in technology, heightened regulatory scrutiny, and a burgeoning awareness of

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<sup>6</sup> Shahzad, A., M., Rutherford, M., A., Sharfman, M., P.: Stakeholder-centric governance and corporate social performance: A cross-national study, *Corporate Social Responsibility and Environmental Management*, 23(2) 2016, pp. 100-112.

sustainability and social responsibility<sup>7</sup>. Far from being a mere rigid framework of rules and procedures, modern governance must adapt to new economic, technological, and societal realities, and the new nature of business. Therefore environmental, social, and governance (ESG) reporting becomes an important part of corporate disclosure, as well as a tool to gain and sustain a competitive edge in the contemporary business reality dominated by millennials and Zs as the lead generations highly sensible to ESG expectations and oriented towards sustainability.<sup>8</sup>

Corporate governance refers to the set of rules, practices, procedures, and processes that guide the direction and control of a company. “With the right structure and systems in place, good corporate governance enables companies to create an environment of trust, transparency and accountability, which promotes long-term patient capital and supports economic growth and financial stability”<sup>9</sup>. Corporate governance entails the delicate balance of interests among numerous stakeholders, including shareholders, management, customers, suppliers, employees, government entities, and the broader community. Effective governance seeks to reduce the inherent management-principal agency relations issues and conflicts within corporate structures, as well as to create an atmosphere where decisions and behaviours of senior executives accord with objectives of the company, shareholders, and important stakeholders, while minding the environment and social footprint at the same time.

The importance of good governance is emphasized by the recent launch of the new governance ISO 37000:2021 guidelines<sup>10</sup>. They are stressing out responsible, effective, and ethical governance that not only fosters an environment of trust, transparency, and accountability but helps align a company’s purpose with the interests of society. Besides, the importance of good corporate governance practices is vital in an era of hypermediatization. Harvard Law School Forum on Corporate Governance – HLSFCG<sup>11</sup> mentions that 64% of investors believe weak governance practices are the most crucial factor, alongside poor financial performance when making investment decisions. Thus, boards

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<sup>7</sup> Lumorous: *The Changing Face of Corporate Governance: A Comprehensive Guide to Implementing Modern Effective Corporate Governance*, 06.06.2024.

<sup>8</sup> For more details on this matter see Tomšić, D.: *Corporate governance challenges – Dealing with unforeseen calls for agile board capabilities*, *Corporate Board: Role, Duties and Composition*, 18(1) 2022, pp. 4-6.

<sup>9</sup> OECD: *G20/OECD Principles of corporate governance*, Paris: OECD Publishing, 2023.

<sup>10</sup> International Organization for Standardization: *ISO 37000:2021 Governance of organizations – Guidelines*, Geneva: International Organization for Standardization, 2021.

<sup>11</sup> Harvard Law School Forum on Corporate Governance HLSFCG: *Global Corporate Governance Trends for 2024*, 06.03.2024.

should ensure better stakeholder reporting, and bear in mind that the board culture boost a company's reputation as well.

Nowadays, corporate governance is to be agile and dynamic.<sup>12</sup> Dealing with unforeseen calls for agile board capability<sup>13</sup>, boards and businesses they oversee face new demands from their stakeholders each year. In line with Connan<sup>14</sup>, the governance of tomorrow should integrate adaptability, agility, collective intelligence, technology, sustainability and social responsibility, so enabling companies to better cope with the future challenges and thrive in the long term. Thus, recognised purpose, aligned goals, fair treatment and ethical behaviour are essential for the introduction of sustainable decision-making in governance practice, aimed at long-term value creation and companies' resilience.

According to the Harvard Law School Forum on Corporate Governance and Russell Reynolds Associates – RRA<sup>15</sup> corporate governance and demands on corporate leaders vary significantly from country to country, but four topics stand out as most important to businesses and their boards across the globe in 2024: (1) disruptive innovations: AI and other technologies rise to the forefront; (2) path to parity: sustained global focus on diversity; (3) more action – and less talk on ESG initiatives; (4) governance standards migrate: private looks to public. Moreover, the increased demand for forward-looking board effectiveness is going on, so as the advancements in AI, quantum computing, and other technologies that, coupled with growing information security and privacy threats, make the front of mind for business leaders and stakeholders. While many of these issues have been on board agendas for years, discussions around these topics skyrocketed in 2023, partly due to the proliferation of generative AI tools like ChatGPT. Moreover, boards around the world are spending more time on their own composition, seeking to build and support boards with important subject-matter expertise, international perspectives, cultural and social diversity, and generational balancing. Many markets have seen a dramatic growth in gender diversity on their boards in recent years and the first political and economic competition is ongoing within the ESG arena, the

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<sup>12</sup> For more details on this matter see Tipurić, D., Tomšić, D.: Agile governance capability, in Tipurić, D., Cindrić, L. (eds.): *Proceedings of the 9<sup>th</sup> International OFEL Conference on Governance, Management and Entrepreneurship* (pp. 99-114), Zagreb, Croatia: CIRU – Governance Research and Development Centre, 2021.

<sup>13</sup> Tomšić, D.: Corporate governance challenges – Dealing with unforeseen calls for agile board capabilities, *Corporate Board: Role, Duties and Composition*, 18(1) 2022, pp. 4-6.

<sup>14</sup> Connan, Y., The Evolution of Corporate Governance: Key to Long-Term Prosperity, 19.09.2024.

<sup>15</sup> Russell Reynolds Associates: Corporate governance trends in the United States, 2024.

popular shorthand for measuring and managing a company's environmental, social, and governance performance<sup>16</sup>.

According to Eccles<sup>17</sup>, the main challenge is whether to use single materiality (which focuses on shareholder value) or double materiality (which includes societal impact), so he recommends a pragmatic approach for corporate leaders: to clearly define corporate purpose, to improve transparency in ESG reporting, and to engage stakeholders constructively. These strategies can help companies manage ESG pressures by focusing on material issues that affect shareholder value while also acknowledging and addressing broader societal impacts. It is worth noticing Hunt's<sup>18</sup> observation that although ESG issues increasingly dominate the agenda, not all three elements receive equal attention. Emphasizing the S in ESG is about making a social impact and purpose as the guiding lights of the corporate strategy. Although stakeholder capitalism has become a kind of buzzword for businesses that strive to achieve more than profits and a high stock price, the real issue still lies in the trade-offs between short-term and long-term perspectives. However, the aim of good governance today is to align stakeholder and shareholder interests in the long term, while it is hard to satisfy every stakeholder group in the short term. So, according to Hunt<sup>19</sup>, the crystallizing concept is purpose-driven ESG.

### **3. THE EVOLUTION AND ONGOING SUSTAINABILITY CHANGES**

Changes in the purpose of the company, as well as in its operating modes and governing principles can arise from numerous and varied exogenous and endogenous reasons. As the global social, environmental, and governance context changes over time, related stakeholder priorities also shift, and consequently, corporate governance practices evolve. Stakeholder expectations regarding social and environmental responsibility continue to grow, so companies should integrate the relevant ones into their governance practice as well as put more effort to meet the expectations of customers, investors, and society at large. Especially through sustainability reporting of organizations, the progress and implementation of sustainable development goals linked to the EU, national, and sectoral achievements can be monitored.

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<sup>16</sup> Harvard Law School Forum on Corporate Governance HLSFCG: *Global Corporate Governance Trends for 2024*, 06.03.2024.

<sup>17</sup> Eccles, R. G.: *Moving Beyond ESG*, *Harvard Business Review*, (September-October) 2024.

<sup>18</sup> Hunt, V.: *Emphasizing the S in ESG*, McKinsey & Company, 05.01.2022.

<sup>19</sup> Hunt, V.: *Putting stakeholder capitalism into practice*, McKinsey & Company. 07.01.2022.

Sustainable development (SD) as a concept refers to balanced and responsible development that meets the needs of current generations without compromising the ability of future generations to meet their own needs. It assumes that it is possible to achieve economic growth and development while preserving natural resources and protecting the environment. Sustainable development was defined in the 1987 Brundtland Report of the World Commission on Environment and Development. Today, sustainable development is an important element of the policies and strategies of almost every country and international organization, with the aim of balancing environmental, economic and social needs for current and future generations.<sup>20</sup>

A milestone in sustainable development and its acceptance was the launching of the 2030 Agenda for sustainable development, a document adopted by the members of the United Nations in 2015. The goal of this comprehensive plan is to improve global sustainable development by 2030. It includes 17 goals, while each of these goals has its own specific sub-goals, a total of 169 of them. The 2030 Agenda focuses on people, the planet, prosperity, peace and partnership, expecting countries to do everything in their national capacities to “leave no one behind”.<sup>21</sup>

In a brief mirroring view<sup>22</sup>, sustainable development has become ubiquitous development paradigm, although a clear definition of this concept and explanation of its key dimensions are not quite academically agreed.<sup>23</sup> Mensah research paper finds that the entire issue of sustainable development centres around inter- and intragenerational equity anchored essentially on three distinct but interconnected pillars, namely the environment, economy, and society. Accordingly, the decision-makers need to be constantly mindful of the relationships, complementarities, and tensions between these pillars and ensure responsible human behaviour and actions at the international, national, business, community and individual levels to uphold and promote the tenets of sustainable development in the interest of human development. Therefore,

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<sup>20</sup> For more details on this matter see Jervie, M., E.: Brundtland Report, World Commission on Environment and Development, Britannica, 2014.

<sup>21</sup> For more details on this matter see United Nations Department of Economic and Social Affairs: *Transforming our world: the 2030 Agenda for Sustainable Development. Resolution adopted by the General Assembly on 25 September 2015 (A/RES/70/1)*, United Nations publication, 2015.

<sup>22</sup> For more details on this matter see Mensah, J.: Sustainable development: Meaning, history, principles, pillars, and implications for human action: Literature review, *Cogent social sciences*, 5(1) 2019, pp. 1653531.

<sup>23</sup> For more details on this matter see Giovannoni, E., Fabietti, G., What is sustainability? A Review of concepts and its applicability, *Integrated Reporting: Concepts and Cases that Redefine Corporate Accountability*, 2013, pp: 21-40.

sustainable decision-making involves considering the long-term impact of choices on the environment, society, and the economy. It starts by setting clear sustainability goals and objectives.

Hence, more needs to be made by the duty-bearers: the UN, governments, private sector and civil society in terms of resource management, policies, education, and regulation to ensure that everyone is sustainable development aware, conscious, cultured and compliant. In this vein, OECD has responded with renewed G20/OECD governance principles and guidelines that corporate sector complies worldwide. The principles are presented in six chapters: (1) ensuring the basis for an effective corporate governance framework; (2) the rights and equitable treatment of shareholders and key ownership functions; (3) institutional investors, stock markets, and other intermediaries; (4) disclosure and transparency; (5) the responsibilities of the board; and (6) sustainability and resilience. Moreover, the corporate sector has to deal with new institutional requirements respectively, for the European Union is facing the new declared regulations on sustainability reporting, so the new directives as well as nature restoration regulation, digital acts, and geopolitical instability are in focus at the EU boardrooms. Hence, the clear and mindfully communicated purpose of the organization could be an overarching umbrella that entails all those “horns in the corporate governance bags”. While corporate social responsibility (CSR) continues to be an important topic, according to Harvard Law School Forum on Corporate Governance and Russell Reynolds Associates, the CSRD and CSDDD will have a direct impact in corporate governance within a volatile business environment that faces geopolitical issues, rapid development of information technology, and climate pressure.

Namely, at the beginning of 2023, the new Corporate Sustainability Reporting Directive (CSRD) entered into force<sup>24</sup>, replacing the Non-Financial Reporting Directive (NFRD) with the deadline for harmonization of national legislation by July 2024 for all EU Member States. CSRD represents a significant step towards the integration of sustainability into business reporting, enabling better transparency and accountability of business entities within the EU, and was launched due to the escalation of climate and environmental challenges with the aim of accelerating the transition of companies to sustainable business models, necessary to achieve Europe’s climate neutrality by 2050. Achieving the ambitious goal of climate neutrality is aimed at transforming for a

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<sup>24</sup> European Commission: 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 Directive 2013/34/EU with regard to corporate sustainability reporting, <[https://finance.ec.europa.eu/capital-markets-union-and-financial-markets/company-reporting-and-auditing/company-reporting/corporate-sustainability-reporting\\_en](https://finance.ec.europa.eu/capital-markets-union-and-financial-markets/company-reporting-and-auditing/company-reporting/corporate-sustainability-reporting_en)>.

sustainable future and requires a comprehensive transformation of the European economy and society. In the process of shaping the climate-resilient economy, a key role falls on businesses, which must transform their business models into climate-neutral or even climate-positive by 2050. The directive applies to all large companies, as well as certain listed SMEs (except micro-enterprises). It requires an audit of the reported information, introduces more detailed reporting requirements and requires reporting according to mandatory EU sustainability reporting standards. The objectives are to increase transparency, which means improving the quality and comparability of sustainability information that companies publish, then supporting sustainable finance, which means ensuring that investors and other stakeholders have access to reliable information on sustainable company practices and improving accountability in terms of promoting sustainable business practices and to increase society pressure on businesses to adopt more sustainable business models and practices.

The key elements of the Directive relate to: (1) reporting coverage: all large companies within the EU, including public companies (more than 250 employees, turnover above EUR 40 million or total assets above EUR 20 million). Small and medium-sized listed companies will also be obliged to report, but with simplified requirements; (2) standardization of reports: introduction of the obligation to use European Sustainability Reporting Standards (ESRS). The reports must include information on the environmental, social and governance impact of the business (ESG criteria); (3) audit and quality assurance: mandatory audit and certification of sustainability information by independent audit bodies to ensure the accuracy and credibility of the reports; and (4) digital reporting: obligation to submit reports in digital format to facilitate data availability and analysis.

What happens next is a new set of regulations for the businesses already visible on the horizon: the forthcoming challenge posed by the European Commission is CSDD Directive that aims to bring a more comprehensive and mandatory approach to sustainability reporting<sup>25</sup>. This Directive establishes a corporate due diligence duty. The CSDDD mandates companies to identify, mitigate, and report on the impact of their operations and supply chains on human rights and the environment. This mandatory legislation, set to take effect by 2025 or 2026, applies to both EU and non-EU companies operating in the EU and mainly targeting those in high-risk industries. The CSDDD will directly apply to both EU and non-EU companies: the Directive applies to EU-based companies with over 500 employees and a turnover exceeding €150M. Alternatively, companies with over 250 employees and a €40M turnover also fall under the

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<sup>25</sup> European Commission: *Directive (EU) 2024/60 on Corporate Sustainability Due Diligence*, Brussels: European Commission, 25.07.2024.

Directive, provided that 50% of their revenue comes from high-risk industries like fashion, minerals, or agriculture. Non-EU companies operating within the EU also fall under the scope of the CSDDD. This includes third-country companies active in the EU that meet the turnover thresholds aligned as mentioned above and the revenue being generated in the EU, irrespective of whether they have a branch or subsidiary in the region. The financial sector has been excluded from CSDDD for now, despite being included in the existing sectoral OECD guidelines.

In its core elements, the CSDDD mandates that companies fall under its scope: (1) identify the principal adverse impact on the environment and human rights resulting from their operations, subsidiaries, and supply chains; (2) mitigate identified risks within their operations and supply chain, support by an action plan and a timeline to address the identified risks; (3) establish grievance mechanisms for workers and stakeholders to raise issues if they arise; (4) align their business model and strategy with the 1.5°C target of the Paris Agreement, specifically for large companies; and (5) publicly report on their due diligence via a sustainability report or website. The core benefits of the CSDDD for citizens are: better protection of human rights, including labour rights; healthier environment for present and future generations, including climate change migration; increased trust in businesses; more transparency enabling informed choices; better access to justice for victims and for companies; harmonized legal framework in the EU, creating legal certainty and level playing field; greater customer trust and employees' commitment; better awareness of companies' negative human rights and environmental impacts, less liability risks; better risk management, more resilience and increased competitiveness; increased attractiveness for talent, sustainability-oriented investors and public procurers; increased incentives for innovation; and better access to finance.

All in all, the elaborated evolutionary steps in sustainable development have obviously influenced and consequently moderated the corporate governance practice: while the great part of the adjustments were mandatory, some companies have applied augmented responsibility requirements of the institutional and regulatory framework, so to sustain their own matching values and purpose, and strengthen company's competitiveness and resilience. Whatever the reason, whether the improvement of the existing corporate governance practice has occurred from the mindful normative or instrumental view of the new way of doing business, corporate governance practices have already upgraded: the compliance with the sustainability rationality increases and the ongoing rise of integrated reporting should serve as the reinforcing mechanism for making more progress along the sustainability trajectory.

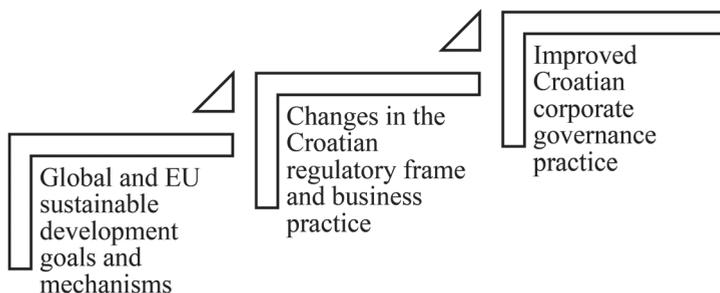
## 4. RESEARCH PROBLEM AND METHODOLOGY

The aim of the analysis is to examine the moderation effect of the sustainable development on governing practice in Croatia. The research is dealing with the national implementation of sustainable development goals level, and its influence on the evolution of corporate governance practices in Croatia, in particular the incorporation of the social and environmental goals into the companies' activities and operations.

### 4.1. RESEARCH PROBLEM

The research problem is to outline the interconnectedness of the ongoing changes in corporate governance practice and sustainable development initiatives and goals. In addition, the challenge of this research is to analyse the state of transparency in companies' sustainability reporting in Croatian companies, measured by the application of the provisions of CSRD. We assumed that by inspecting the communication of the companies that focuses on or is dealing with corporate governance practices, we could grasp the state of the sustainability level implemented in corporate governance practice. The research model is presented in Figure 1 below.

**Figure 1. Research model**



Source: authors

As depicted in the research model, we assume that the global and EU sustainable development goals and related mechanisms in the forms of directives induce direct changes in the Croatian regulatory frame and business operations, which in turn lead to the improved corporate governance practice in Croatia. Hence,

Hypothesis 1: Croatian sustainability practice has moderately improved in the last two decades.

Hypothesis 2: Croatian corporate governance practice has moderately improved by the provision of the CSRD and forthcoming provision of the CSDDD.

#### *4.2. RESEARCH METHOD AND SAMPLE*

For our research, we chose the Word Cloud method and applied it on the sample of 100 largest Croatian companies, ranked by Fina, based on the top revenue reached in 2023<sup>26</sup>. The research was conducted in the form of inspecting publicly available reports and web sites content of the companies.

Word clouds are increasingly being used within the public and private sectors as a tool to identify the focus of written material. A Word Cloud is described as a visual representation of word frequency derived from written text. According to Attenstaedt<sup>27</sup>, it reveals the most prominent words that are associated with the content of research. The more often the word appears within the passage being analysed, the larger it appears in the image generated. McNaught and Lam<sup>28</sup> highlight that this approach provides viewers with a selection of the themes/worlds contained within the text. As research tools, Word Clouds have several limitations, since they fail to group words that have the same or similar meaning, and the words that are retrieved out of context as the technique omits the semantics of the words, as well as the phrases they comprise. However, the method demonstrates a fast and visually rich way to enable researchers to gain the basic understanding of the data at hand. Word clouds can be a useful tool for preliminary analysis and for validation of previous findings, as well as for the sense, the sentiment or the tone of the written content. Nonetheless, Word Cloud is a popular adjunct method, but if used as a stand-alone research tool, it is not comparable to the traditional content analysis methods due to its shortcomings.

The key words that we were looking for in our web pages inspection were key words aligned with SD, CSRD and CSDDD. We were open to the selection of other commonly used words related to the nonfinancial reporting and disclosure or ESG, as well as the projects that relate to the subject of the matter. We have structured our research with three supporting questions:

1. How many companies have a sustainable business or corporate sustainability label on their websites;

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<sup>26</sup> <<https://www.fina.hr/>>, last accessed on 30/08/2024.

<sup>27</sup> For more details on this matter see Attenstaedt, R., Word cloud analysis of the BJGP, *British Journal of General Practice*, 62(596) 2012, pp. 148; Attenstaedt, R., Word cloud analysis of the BJGP: 5 years on, *British Journal of General Practice*, 67(658) 2017, pp. 231-232.

<sup>28</sup> For more details on this matter see McNaught, C., Lam, P.: Using Wordle as supplementary research tool, *Qualitative Report*, 15(3) 2010, pp. 630-643.

2. The most common words repeated by all sampled companies; and
3. Other words or projects related to the research topic.

## 5. RESEARCH FINDINGS AND DISCUSSION

Our initial assumptions about the state of the sustainability level implemented in corporate governance practice in Croatia were not ambitious. The research findings show that the Croatian business sector is not agile in web communication but seems aware of the forthcoming wave of changes that the CSRD and CSDDD bring.

### 5.1. RESEARCH RESULTS

Surprisingly, the answers to our first research question were more than modest:

**Q1:** How many companies have a sustainable business or corporate sustainability label?

- sustainable business – 2 companies (2%)
- corporate governance – 9 companies (9%)
- corporate sustainability – 0 companies (none).

From the results presented above, the state of the Croatian biggest companies in terms of communication dealing with sustainability is below the expectations. The Croatian business sector is not agile in web communication and not quite transparent. The finding is worrying since those companies are the national best that should be regarded as a kind of role models for the other companies, and set the path and lead the way, which they are obviously not doing.

**Q2:** The most common generic words repeated by all sampled companies are presented in Table 1. below.

**Table 1. The dominant words for the Sustainability-Governance Word Cloud**

KEY WORD	NUMBER OF COMPANIES	PERCENTAGE OF COMPANIES (%)
ENVIRONMENT	26	26%
EMPLOYEES	16	16%
CLIMATE CHANGE	3	3%
ANTI-CORRUPTION	6	6%
VENDORS	5	5%
SUSTAINABILITY	23	23%

Source: authors' calculation

Table 1 shows the generic keywords related to the topic that are present in all the analysed companies and the frequency of occurrence of each keyword: 26% of companies use the word environment; 16% use the word employees, 14% use the word climate change, anti-corruption and suppliers, and 23% of companies use the word sustainability.

**Q3:** Segmentation of other specific words that dominate as well as projects related to CSR, CSDDD and SD are presented in Table 2. below.

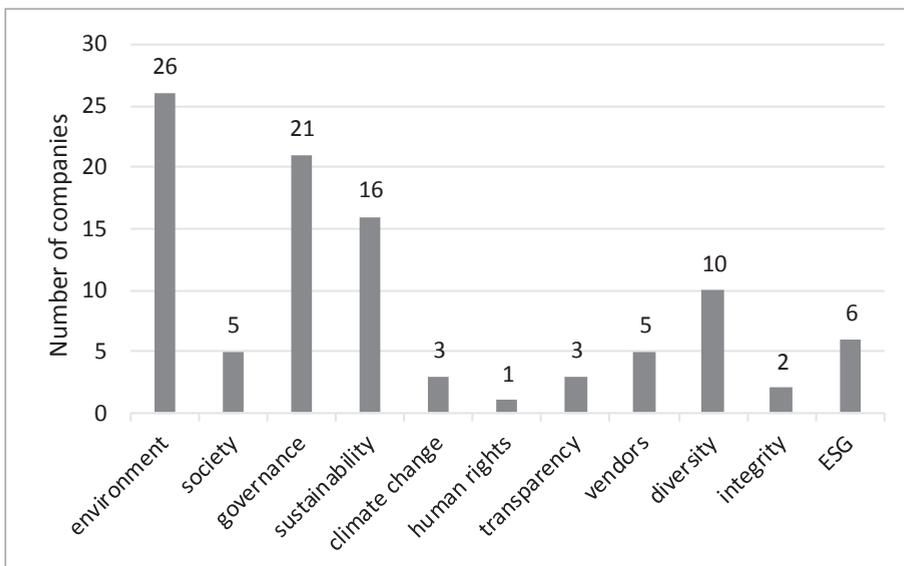
**Table 2. The frequent specific words for the Sustainability-Governance Word Cloud and related projects**

Specific words related to CSR, CSDD and ESG	Number of companies	Percentage	Published reports in corporate sustainability in accordance with directives	Number of companies	Percentage
environment	26	26%	Sustainability reports	4	4%
society	5	5%	Sustainability strategy	2	2%
governance	21	21%	Sustainability project	2	2%
sustainability	16	16%	Risk management	6	6%
climate change	3	3%	Social responsibility	3	3%
human rights.	1	1%			
transparency	3	3%			
vendors	5	5%			
diversity	10	10%			
integrity	2	2%			
ESG	6	6%			

Source: authors' calculation

Table 2 reveals the most prominent words that are associated with the content of research and constitute the Word Cloud: environment – especially renewable energy sources, management and sustainability. There is also an interest in social topics such as diversity. When reporting, in addition to sustainability reports which are only now becoming an obligation for medium and small enterprises, companies pay attention to risk management reports. The following Graphs 1 and 2 depict the research findings more clearly.

**Graph 1. Specific words related to CSRD, CSDDD and SD**



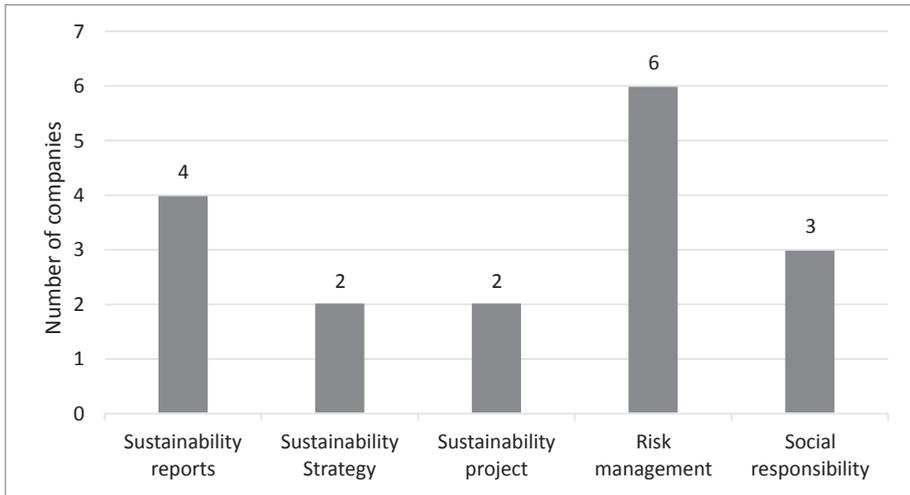
Source: authors' calculation

Graph 1 shows the frequency with which certain words or terms are associated with companies in the context of CSRD, CSDD and SD. The height of the column shows how many times the word is mentioned in relation to the analysed companies.

The most frequently mentioned words are “environment” and “society”, which indicates the great importance of environmental and social aspects of business for companies that adhere to CSRD standards. This suggests that these companies are aware of their impact on the environment and society and are taking measures to reduce negative impacts and increase positive ones. The words “governance” and “sustainability” are also frequently mentioned, highlighting the importance of good governance and long-term business sustainability. This suggests that businesses understand that sustainability is not just a matter of the environment and society but requires a comprehensive approach that includes economic sustainability. Graph 1 also reveals that businesses address a wide range of ESG topics, including climate change, human rights, transparency, suppliers, diversity and integrity. This suggests that companies are aware of the complexity of the ESG and seek to cover all relevant aspects in their activities. Some topics, such as “human rights” and “transparency”, although important, are mentioned less frequently. This may indicate that there is room for improvement in these areas or that some businesses may be more focused

on other aspects of the ESG. The research below also shows how companies currently deal with CSRD, CSDDD and ESG topics. The findings of the research in this area are provided by Graph 2.

**Graph 2. Published reports in corporate sustainability in accordance with the directives**



Source: authors' calculation

Graph 2 provides useful insights showing how companies deal with CSRD, CSDD and SD topics and shows the number of companies that have published different types of sustainability-related documents, in line with the applicable directives. Document types are, as follows:

- Sustainability reports: These are comprehensive documents that show how the company affects the environment, society and the economy, and what measures it takes to reduce negative impacts and increase positive ones.
- Sustainability strategy: This document outlines the company's long-term sustainability goals and how these goals will be achieved.
- Sustainability project: These are specific projects that a company implements to achieve its sustainability goals.
- Risk management: This document describes how the company identifies, assesses and manages sustainability-related risks.
- Social responsibility: This document focuses on social aspects of sustainability, such as stakeholder relations, labour and human rights.

It can be concluded from Graph 2 that the largest number of companies have published sustainability reports as well as risk reports. This indicates that businesses are aware of the importance of transparency and reporting on their sustainability activities. Fewer companies have formal strategies and projects. Namely, although most companies publish reports, a small number of them have a detailed strategy and specific projects to achieve their sustainability goals. However, risk management reports are significantly represented, indicating the awareness of the company's management about the need to manage the company's resilience. Social responsibility is an aspect of sustainability that is less represented in the reports, which indicates that companies still do not pay enough attention to this area, so there is room for improvement. Businesses should develop more detailed strategies, launch more sustainability related projects and pay more attention to sustainability and social responsibility if they aim at strengthening company's strategic posture and encourage stakeholder groups such as investors, customers and employees to assess and value the company's commitment to sustainability. Companies with detailed reports, strategies and projects are more attractive to stakeholders focused on sustainable financing as well as sustainable investments. This graph provides valuable insight into the current state of sustainability reporting in Croatian top 100 companies.

## *5.2. DISCUSSION*

The research findings reveal that Hypothesis 1: Croatian sustainability practice has moderately improved in the last two decades is sustained. More elaboration is highlighted below.

As an EU member, Croatia adopts the policies and goals of sustainable development defined at the European level and transfers them to the national level aimed at achieving sustainable development through the adoption of policies, programmes and initiatives that support a balance among social, economic and environmental objectives. Croatia has its National Development Strategy 2030, the first comprehensive and systematic strategic planning act that provides strategic guidance and forms the basis for the design and implementation of all public policies at national and sub-national level, and promotes a balance of economic, social and environmental development. Four development directions and 13 associated strategic goals have been defined, which will contribute to the accelerated and sustainable growth and development of Croatia, i.e. the realization of Croatia's vision until 2030. The four development directions are: (1) sustainable economy and society; (2) strengthening the resilience to crises; (3) green and digital transition; and (4) balanced regional development, while the related goals are the following: competitive and innovative economy,

educated and employed people, efficient and effective judiciary, public administration and management of state property, global recognition and strengthening of the international position and role of Croatia, healthy, active and quality life, demographic revitalization and better position of families, security for stable development, ecological and energy transition for climate neutrality, food self-sufficiency and development of the bioeconomy, sustainable mobility, digital transition of society and economy, development of assisted areas and areas with development specificities and strengthening regional competitiveness.

Achieving the set strategic goals and coordinated implementation of policies in the four development directions will contribute to the realization of the national vision according to which Croatia in 2030 is an open and globally competitive country whose social and economic growth and development are based on sustainable development. The established development directions and strategic goals should contribute to Croatia making the best use of its potential, to eliminate the economic and social damage caused by the global crisis and to encourage the fastest possible recovery. This considers the goals set under the United Nations 2030 Agenda for Sustainable Development, the European Green Deal and the European Territorial Agenda 2030. All this forms the basis for sustainable, inclusive and innovative development of Croatia, while achieving the resilience of society and the economy to global crises.

The European and national sustainability reports serve as an important tool in monitoring progress, identifying challenges and guiding policies and practices towards achieving the sustainable development goals (SDGs), and provide insight into achievements, challenges and areas for further work. According to the Report of the Government of the Republic of Croatia on Sustainable Development for 2023<sup>29</sup> Croatia ranks 12th out of a total of 166 countries for which data collection on the performance of the implementation of the SDGs has been conducted, and in the last five years there has been visible progress in number of areas. Progress is particularly visible when it comes to reducing poverty and social exclusion (SDG 1), ensuring economic growth and development (SDG 8), and implementing policies aimed at reducing inequalities or improving living conditions, especially for the most vulnerable and vulnerable groups of the population (SDG 10). When it comes to the green transition, Croatia is making significant efforts to ensure an increase in the capacity of renewable energy sources. The share of renewable energy in total final energy consumption in Croatia is above the EU average. Significant efforts are also being made in the decarbonization of the energy sector and the economy, as well as in the security of energy supply with the aim of providing citizens with

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<sup>29</sup> Vlada Republike Hrvatske: *Dobrovoljni nacionalni pregled o provedbi ciljeva Programa Ujedinjenih naroda za održiv razvoj do 2030.*, lipanj 2023.

clean, sustainable and affordable energy (SDG 7). As a leading Member State of the European Union in terms of water supplies, Croatia is fully committed to the mission of preserving this natural treasure. Thus, significant progress is also visible in the field of ensuring access to safe, i.e. drinking water and water management (SDG 6). Great efforts are being made to combat climate change (SDG 13), with Croatia aiming to reduce its greenhouse gas emissions to at least 65% of 1990 levels by 2030. In addition to the present climate challenges, Croatia is focusing great efforts on the conservation of the marine environment (SDG 14) and biodiversity (SDG 15), and it is important to point out that Croatia is ranked 3rd in the EU in terms of the area covered by forests.<sup>30</sup>

The 2023 report of the European Commission for Croatia also shows progress in achieving all sustainable development goals in the last five years. In eight objectives, Croatia is above the European Union average with positive progress, namely: quality education (SDG 4), clean water and sanitation (SDG 6), affordable and clean energy (SDG 7), reducing inequalities (SDG 10), life on land (SDG 15), industry, innovation and infrastructure (SDG 9), decent work and economic growth (SDG 8), peace, justice and strong institutions (SDG 16), while in nine objectives such as a world without poverty (SDG 1), a world without hunger (SDG 2), the development of human health and well-being (SDG 3), sustainable cities and communities (SDG 11), climate action (SDG 13), life under water (SDG 14), responsible consumption and production (SDG 12), gender equality (SDG 5) and partnership (SDG 17), although continues to make positive progress, Croatia is still below the EU average.<sup>31</sup>

An important source that measures overall progress towards achieving all 17 SDGs is the Europe sustainable development report. The report highlights areas of success as well as opportunities for further improvement and uses the data to compare the progress of European sub-regions. From 2019 The Report on Sustainable Development in Europe presents the Sustainable Development Index and Dashboards for Europe and provides an annual overview of the European Union's progress towards the SDGs, as well as the progress of 38 individual European countries, including all EU countries, EU candidate countries and regional partner countries. The goals of the SGD Agenda 2030 are also indicators of sustainable development of SDI<sup>32</sup>. The performance of Croatia in the last twenty-three years is shown in Figure 2.

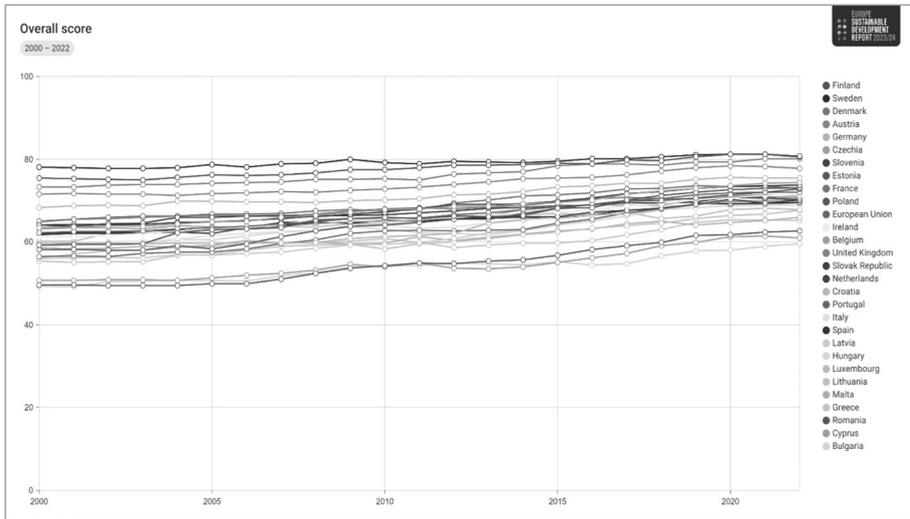
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<sup>30</sup> Vlada Republike Hrvatske: *Dobrovoljni nacionalni pregled o provedbi ciljeva Programa Ujedinjenih naroda za održiv razvoj do 2030.*, lipanj 2023.

<sup>31</sup> Eurostat: *Sustainable development in the European Union. Monitoring report on progress towards the SDGs in an EU context*, 2023 edition, Luxembourg: Publications Office of the European Union, June 2024.

<sup>32</sup> European Sustainable Development Report 2023/24, n.d., <https://eu-dashboards.sdgindex.org/>.

**Figure 2. Performance on the SDG Index: EU average and performance in the EU27 and UK, 2000-2023.**



Source: <https://eu-dashboards.sdindex.org/explorer>

Figure 2 shows the impact of SDG output as measured by the SDG index, which includes the EU average and performance in the EU27 and UK, 2000-2023. Countries are sorted by total score. The overall score measures the overall progress towards achieving all 17 SDGs. The result can be interpreted as a percentage of SDG achievement, so the result of 100 means that all SDGs have been achieved. Figure 2 shows that Croatia was making moderate progress during the observed period, which is more visible in the period since 2015, but it is still at the very back of the observed countries, ahead of Bulgaria, which is the last. Although there is significant room for progress in achieving the SDGs, there is no doubt that their implementation affects the Croatian economy and all business entities. Furthermore, all four development directions from the National Development Strategy 2030 are interconnected and focused on sustainable development. More importantly, the strategy is vertically linked to regional and local development plans that moderate the actions and behaviour of companies operating in Croatia. Encouraging the sustainability of the economy and society, the green and digital transition and, in particular, strengthening the competitiveness and innovation of the economy, also direct legislation towards improvement in such a defined development framework, which consequently improves corporate practice.

Related to Hypothesis 2: Croatian corporate governance practice has moderately improved by the provision of the CSRD and forthcoming provision of the CSDDD, the research findings reveal that the hypothesis is sustained. The elaboration of the finding could be found below:

Globally and locally, the problem of improving corporate governance practices stems from a focus on short-term goals. Namely, according to the report of the European Commission<sup>33</sup>, the focus of corporate decision-makers on short-term shareholder value maximization rather than on the long-term interests of the company reduces the long-term economic, environmental and social sustainability of European businesses. The research analysed the relationship with current market practices and/or regulatory frameworks, and identified possible EU-level solutions, also contributing to the attainment of the UN SDGs and the goals of the Paris Agreement on climate change. The issues contributing to “short-termism” in company law and corporate governance have been indicated and grouped around seven key problem drivers, covering aspects such as directors’ duties and their enforcement, board remuneration and composition, sustainability in the business strategy, and stakeholder involvement. The study suggests that the possible future EU action in the area of company law and corporate governance should pursue the general objective of fostering more sustainable corporate governance and contributing to more accountability for companies’ sustainable value creation.

Following these findings, the new CSRD and the forthcoming CSDDD should rapidly moderate EU and national corporate governance practices. To enable the transposition of CSRD provisions into national legislation, the “hard law” revolution in Croatia has occurred recently. The Parliament of the Republic of Croatia has adopted amendments to the Audit Act, the Accounting Act and amendments to the Capital Market Act. The first sustainability reports under the new Accounting Act will be published in 2025 for 2024. Gradually, the sustainability reporting obligation will cover all large entrepreneurs and small and medium-sized enterprises whose securities are admitted to the EU regulated market.

As stated in the research findings, the Croatian business sector is not agile in web communication but seems aware of the forthcoming wave of changes that the CSRD and CSDDD bring. According to the research findings, the key words that make a country specific Sustainability-Governance Word Cloud are environment, governance, sustainability, diversity and ESG. From the Word

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<sup>33</sup> European Commission Directorate-General for Justice and Consumers: *Study on directors’ duties and sustainable corporate governance: final report*, Brussels: Publications Office, 2020.

Cloud, one can assume that the top researched Croatian companies are trying to send the message that they are modestly supporting the initiative of corporate augmented responsibility. So, the state of the CSRD requirement in Croatia could be qualified as moderately improving. Only 17 companies have published some kind of sustainable reports, which can be considered a small number, regardless of the fact that the full reporting profile according to CSRD provisions was not an obligation during the research period. An even more devastating result of the research is related to the existence of sustainability layers on websites. In doing so, companies neither contribute to the transparency of information nor pay due attention to the communication towards stakeholders on sustainability issues. On the other hand, one of the positive findings is the Corporate Governance Codes/Codes of Ethics that are represented on most websites, and not only of the companies listed on the regulated capital market, which is an obligation imposed in Croatia by the HANFA regulator.

According to the authors, the Corporate Governance Codes as “soft law” tools will be significantly amended and harmonized with the provisions of the CSRD and CSDDD directives. Furthermore, the authors point out that there is no designated supervisory authority yet in Croatia that will oversee the sustainability and, consequently integrated reports. The expectation is to appoint a body that already supervises the financial statements – HANFA (Croatian Financial Services Supervisory Agency). If so, its scope of work should be expanded in the direction of monitoring corporate sustainability. This will, no doubt, not only moderate, but significantly improve the practice of corporate governance in Croatia.

In support of the hypothesis that the practice of corporate governance is moderately improved by the provision of the CSRD and the forthcoming provision of the CSDDD, it is worth highlighting the results of the research on the quality of corporate governance in Croatia. Corporate governance quality is commonly evaluated using a comprehensive measure as an index, like SEECGAN<sup>34</sup>. The SEECGAN index consists of questions covering seven key areas of corporate governance: corporate reporting, ownership concentration of shareholder rights, boards (number, size, composition, expertise), rewards and compensations, social responsibility, audit and internal control and corporate risk management. Findings from the research conducted in 2024 on a sample of 58 companies listed on the Zagreb Stock Exchange indicate that the quality of corporate governance within these companies falls below satisfactory levels, with the SEECGAN Index averaging at 4.97, less than half of its

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<sup>34</sup> Tipurić, D. et al.: *Korporativno upravljanje u Hrvatskoj – Ocjena kvalitete korporativnog upravljanja hrvatskih dioničkih društava SEECGAN metodologijom*, Zagreb: CIRU – Centar za istraživanje i razvoj upravljanja, 2015.

maximum 10 score of the potential value<sup>35</sup>. Nevertheless, the corporate governance quality level has improved for more than the index point (3.91) in the last 9 years compared to the overall Croatian score for the listed companies at that time.<sup>36</sup> However unsatisfactory the contemporary results may seem, progress and improvements can still be seen, with the expectation that from next year, this index will also show improvements in corporate governance practices, especially in corporate reporting.

## 6. CONCLUSION

The evolution of corporate governance is a continuous journey that requires constant adaptation and openness to change. Governance focused on sustainability not only enhances the company's reputation but also fosters its long-term resilience. The research results show that the evolution of sustainable development, measured by the level of national implementation of sustainable development goals, has influenced the evolution of corporate governance practices in Croatia by incorporating social and environmental goals into the creation of added value for companies. The newly shaped country-specific Croatian Sustainability-Governance Word Cloud shows that environment, governance, sustainability, diversity and ESG make the core of corporate communication on sustainability today. By highlighting those words, one can conclude that the changes in the focal communication on corporate governance also moderate the national corporate practices.

The authors deem that the new CSDD Directive will bring issues in the implementation and reporting process, in particular regarding the understanding of the extended liability of companies outside their borders which they cannot directly control. Another issue that is an old one but transcends to a new level is the divergent stakeholder's interest. Nevertheless, corporate sustainability should become an anchor of corporate and business strategies. Moreover, collaborative strategies<sup>37</sup> can help find a balance between the diverse goals of important company stakeholders, since they are specific to each activity and each company. Although the convergence of corporate governance in the EU

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<sup>35</sup> Obuljen, D., Kovač, I., Cindrić, L.: Interdependence of Corporate Governance Quality and Entrepreneurial Orientation of Croatian Companies, *InterEULawEast*, 11(1) 2024, p. 49.

<sup>36</sup> For more details on that matter see Tipurić, D. et al.: *Korporativno upravljanje u Hrvatskoj – Ocjena kvalitete korporativnog upravljanja hrvatskih dioničkih društava SEECGAN metodologijom*, Zagreb: CIRU – Centar za istraživanje i razvoj upravljanja, 2015.

<sup>37</sup> Tipurić, D., Tomšić, D.: Collaborative strategies to heal the competitive paradigm shortcuts, in: Tipurić, D., Kovač, I. (eds.): *Proceedings of the 4th International OFEL Conference on Governance, Management and Entrepreneurship* (pp. 1247-1260), Zagreb: CIRU – Governance research and Development Centre, 2016.

closed market has been going on for some time, the “one size fits all” approach is not a solution to further improve corporate governance practices globally and locally. The best way to understand and harmonize the divergent interests of all stakeholders is through a shared purpose and commitment to sustainable policies and decisions that strengthen the long-term prosperity of a company, without harming the environment and the society. Therefore, a clearly defined and communicated purpose of the company, a change of focus from short-term to long-term goals and collaborative strategies seem to outline an effective framework that supports the development of sustainability and resilience of the company, while at the same time improving the quality of corporate governance practices focused on sustainability issues.

We hope that the paper contributes to the understanding of the interconnection between sustainable development and corporate governance, and consequently, to the development of improved and more sustainable corporate governance practices in Croatia. The research presents empirical findings of the current state of the sustainability-governance communication and so to call disclosure practice in 100 Croatian biggest companies. The mayor shortcoming of our research is methodological robustness. The research lacks expanded contextual analysis as well as the correlation between specific goals from the national strategy and SDG achievement, and national governance practice indicators. To improve the methodological robustness of the future research, qualitative or quantitative methods are recommended. The scientific and applicative implication of the paper could be found in the fact that the first Country-specific Word Cloud is shaped. As for the recommendation for the future research avenues, we suggest shaping of the SC-CG national matrix, so to (re)connect the achievements and the improvement in both fields. Another research trajectory could deal with the redesign of the national and company corporate governance codes. Besides, stakeholder governance, the occurrence that is already becoming the field issue, needs embedding in the shareholder understanding of the board roles, along with the new mechanisms that will enable sustaining of the national and global sustainability goals in a feasible manner.

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