

CORPORATE SOCIAL RESPONSIBILITY

Submission in response to the invitation of the Corporations and Markets Advisory Committee from Henry Bosch AO.

1. The Minister's first term of reference asks whether the Corporations Act should be revised to clarify the extent to which directors may take into account the interests of specific classes of stakeholders or the broader community when making corporate decisions.

Response:

The Act should not be revised for this purpose because directors already take the interests of legitimate stakeholders and the broader community into account and their right to do so is already generally understood. Legislative guidance is not only unnecessary but would impose rigid parameters which would be counter-productive.

I joined my first board [that of John Lysaght Australia Ltd – now part of Blue Scope Steel] in 1972 and, apart from the five years 1985-1990 when I was Chairman of the National Companies and Securities Commission, I have been a director ever since. I have served on over thirty boards and in the last sixteen years have advised scores of others. Moreover I have taught hundreds of groups of directors for the Australian Institute of Company Directors and for other bodies. I have never encountered a board that did not recognise the need to take account of the legitimate interests of stakeholders, and I have never heard it argued that such interests should not be taken into account, or that the existing law was an impediment to doing so.

All boards of which I am aware consider the company's interests in the longer term as well as the short term. Plans, whether they are called Strategic or Corporate or Business, are made in all but the smallest companies and directors look forward to planning horizons which are usually three to five years, but which may extend much further. While planning is done poorly in many companies there is always a recognition that, at least in the longer term, if the company does not look after its customers sales will suffer, if it is regarded as a bad employer it will be harder to recruit good people, if it doesn't pay its debts it won't get credit, and so on. Corporate reputation is a valuable asset and is seen to be so. These matters are almost always taken into account, at least to some extent, in making corporate decisions. Of course short term pressures sometimes prevail, particularly in times of crisis, but if they prevail for long the company will cease to exist.

This experience bears out the thrust of Section 1.3.3 of the Discussion Paper, with which I agree. See especially note 27 on page 12. Several other observations in the Discussion paper are also pertinent.

The fact that directors take account of the interests of genuine stakeholders and the reputation of their companies in the general community does not mean that everyone will always be satisfied. Taking into account is not the same as deciding in favour of. The

interests of some stakeholders will always be opposed to those of others. For example, employees want higher pay, better conditions and secure tenure – all of which raise costs - while customers want lower prices, which require lower costs. Directors are, and will always be, forced to choose between different interests and the only realistic criterion on which they can base their decisions is the long term survival and prosperity of the company. Naturally those who contribute more to the company, those who are more important to its survival and prosperity, will find their interests given greater weight than those who contribute less. Those who would like to be considered stakeholders but contribute little or nothing to the company, such as casual passers-by, like Greenpeace, will always be disappointed and will always be calling for more CSR - by which they mean that they want their interests to prevail.

Professor Berle's comment, quoted at note 8 on page 5 of the Discussion Paper "You cannot abandon the emphasis on the view that business corporations exist for the sole purpose of making profits for their [shareholders] until such time as you are prepared to offer a clear and reasonably enforceable scheme of responsibilities to someone else" is absolute right. The muddled confusion which goes by the name of corporate social responsibility, and which the Advisory Committee cannot define [page 3], is a very long way from being a "clear and reasonably enforceable scheme of responsibilities".

In the last few years a great deal more attention has been paid to stakeholders, and to the supposed interests of the general community, than in the previous decade. There have been significant changes in social attitudes, and a large increase in media attention. In particular, environmental issues have received far more notice than they did a decade ago. It should not be assumed that the present foci of attention are permanent. Intellectual fashions change rapidly and legislators should avoid being trapped in the parochialism of the present. As the historian Lord Macaulay put it: "He alone reads history aright who, observing how powerfully circumstances influence the feelings and opinions of men, how often vices pass into virtues and paradoxes into axioms, learns to distinguish what is accidental and transitory in human nature from what is essential and immutable." The present fashion for corporate social responsibility and environmental concern is not the first [remember the Club of Rome in the 1970s and the pressures which led to the Senate inquiry in the late 1980s], and it is unlikely to last – at least in its present form. Refer to the note 6 on page 3 of the Discussion Paper ["The Cycles of Corporate Social Responsibility: An Historical Retrospective for the Twenty-first Century"].

2. The Minister's second term of reference asks whether the Act should be revised to **require** directors to take stakeholder or community interests into account.

Response:

The Act should not be revised for this purpose because it would undermine the accountability of boards. Unaccountable power tends to corrupt and there have been many instances in which managements and/or boards have done great damage [including harm to stakeholders and the community] as a result of pursuing their own interests. It is

vital that the Corporations Act preserves the clear accountability of boards to some external entity able to hold them to account. Stakeholders and the general community are so diverse that they cannot perform this function. Over the last fifteen years there has been a rapid increase in the ability and preparedness of shareholders to act like owners and there is every indication that this trend is continuing. There are strong reasons for believing that it will continue. Clear responsibility to shareholders for the prosperity of the company in perpetuity is the essential basis of accountability and legislators would be very unwise to tamper with it.

Over the last two decades a great deal of progress has been made in developing corporate governance structures and procedures which reduce the likelihood and scope for the abuse of unaccountable power. A vital element of corporate governance is the recognition that managements are accountable to boards and boards are accountable to shareholders. For accountability to be effective there have to be criteria by which performance can be measured which are clear, simple and straight forward. There is still a lot more to be done in this area and it is important not to blur the issues.

Were directors required to take other interests into account their accountability to shareholders would be diluted and it would be difficult, if not impossible, to show that they were not acting properly. If profits fell it could be claimed that the board had had to give priority to the environment, and if the environment did not receive the attention its advocates wished it could be argued that some aspect of social justice had received priority. The Senate Standing committee on legal and Constitutional Affairs put this well in its 1989 Report "To require directors to take into account the interests of the company's employees, its creditors, its customers or the environment, as well as its shareholders, would be to require them to balance out what would on occasions be conflicting forces....it would also limit the enforceability of shareholders' rights if directors were able to argue that, in making a certain decision, they were preferring other interests." Paragraph 2.20. Other relevant quotations from the Senate Report are included in the Discussion Paper at Section 3.2.2.

The so-called Triple Bottom Line is a serious threat to accountability. Of course, in many cases it is only a public relations exercise but, if boards genuinely claim that their performance should be measured by three separate criteria, that amounts to a dereliction of duty. No common denominator has been, or could be, put forward which would enable the three criteria to be balanced, and being accountable by three independent criteria simultaneously means not being accountable at all.

3. The Minister's third term of reference asks whether companies should be encouraged to adopt socially and environmentally responsible business practices and if so how.

Response:

Section 1.1 of the Discussion Paper outlines the difficulties with the concept of corporate social responsibility and on page 3 it is stated that the Advisory Committee does not propose to adopt a particular definition. That was wise. There are so many different groups with different agendas and concepts claiming to speak in the name of "Corporate Social Responsibility" that the only common denominator is a warm cuddly glow. [See the muddled nonsense included in note 3 on page 2 of the Discussion Paper in the names of Sustainability and the EU Green paper et al].

There is already a great deal of pressure on companies to adopt practices which are regarded as socially responsible by various groups. The emphasis of this advocacy will almost certainly vary as time goes on and circumstances change, and the Government would be well advised to stay clear of the issue. As Bernard Shaw commented [in "Major Barbara"] "For every man there is but one true morality, but every man has not the same true morality."

4. The Minister's fourth term of reference asks whether the Act should require certain types of company to report on the social and environmental impact of their activities.

Response:

The Act should not require special reporting. There is a very great deal of reporting already and it should not be increased because:

1. further reporting would increase business costs and thus add costs to ultimate consumers,
2. statutory requirements are rigid and unlikely to keep up with changing circumstances. They are often only a roadmap for the unscrupulous – they enable companies to comply with the letter while avoiding the spirit of the requirements.
3. reporting can be, and often is, very misleading. The Enron statement on Corporate Social Responsibility was one of the best published by any company but it turned out to have little connection with reality.

Henry Bosch
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