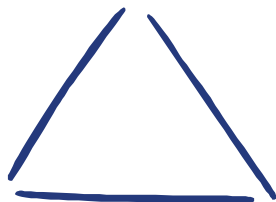


Doughty Centre



Corporate Responsibility

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The Business of Business is...?

Unpicking the Corporate Responsibility Debate

by
Chris Marsden OBE and David Grayson CBE

A Doughty Centre for Corporate Responsibility Occasional Paper

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THE BUSINESS OF BUSINESS IS...? – UNPICKING THE CORPORATE RESPONSIBILITY DEBATE – CHRIS MARSDEN AND DAVID GRAYSON

Executive summary

Companies must be part of any lasting solution to many of the pressing environmental and social problems facing the world. All companies do good things and bad things, often at the same time. The essence of the debate over Corporate Responsibility¹ (CR) is whether governance of the good and bad things companies do should be left to market forces and state regulation or whether companies should deliberately set out to do good things beyond the minimum required to achieve their financial goals.

Those opposed to corporate responsibility from the political 'Left' argue that CR is a business-driven palliative to divert attention from the need for proper, enforceable regulation. Critics from the 'Right' argue that deliberate attempts to manage a company's environmental and social impacts beyond those required by law and market forces, has no legitimacy. Moreover, they argue it risks diverting management's attention from its main task and sphere of competence, and is likely to lead to misguided actions and/or destruction of value.

This paper argues that the 'leave it to market forces within the rules of the game' position may be tenable if the rules are both sound and universally enforced. Under such circumstances CR, beyond obeying the rules and paying taxes, would be largely discretionary. However, there are many instances where the rules are weak and/or not enforced. Since 1989 the nature and effect of globalisation has changed the state of governance radically: firstly, governments alone are less able to manage public interest issues to the extent traditionally expected of them; secondly, the lack of effective governance of global issues is becoming more apparent and urgent; thirdly, companies do business in many weak and failed states where governance is both lacking and often corrupt. Companies are finding themselves caught up in the *de facto* governance of public issues, whether they or the rest of society like it or not. It is therefore incumbent on companies, government agencies and civil society pressure groups to make this new governance reality work as well as possible.

The key question is where this new form of CR is leading. Is it, as those arguing against CR from both the left and right of the political spectrum assert, risking prolonging a period of inadequate governance by letting reluctant state authorities off the hook? Or is it part of an evolving movement towards more effective global governance? The paper argues that CR is an inescapable part of doing business at this time. It is legitimised by the current governance deficit, both globally on some issues and in many states; and by companies' power to make a positive difference, within their spheres of influence, on environmental and human rights issues where they operate. However, all involved in this pragmatic evolution of *de facto* governance processes should consider this – at least theoretically – as an ultimately transitory, if long term, phenomenon. It is further argued that all involved should work together to

¹ For a cross-section of definitions of Corporate Responsibility see:
<http://www.som.cranfield.ac.uk/som/research/centres/ccr/mission.asp> accessed December 20th 2007

assist the development of better *de jure* processes. It is in the long term interests of the companies that are taking a lead in addressing these issues of business to society, to work for a level playing field, on which they can compete fairly with other companies which take a free ride on CR matters. That implies that leading companies and their associations should be actively lobbying governments for better regulation, not less. If and when the governance of company environmental and social impacts is firmly brought within the rules of the game, then CR can perhaps return to being largely discretionary – but that time, if ever, is a long way off.

It remains an open question: in the face of the greatly increased complexity of the issues facing global society, whether governments alone, however well-organised, professional and far-seeing they are, can even theoretically, be able to solve the major environmental and societal issues on their own?

Introduction

This Occasional Paper originated in the 2007 Cranfield MBA students' conference. Cranfield Emeritus Professor David Myddelton and David Grayson, debated the motion that: *"There is only one social responsibility of business – to engage in activities designed to increase profits, so long as it stays within the rules of the game."*

In the course of the debate, and during contributions at the same conference from two other Davids: Prof David Henderson, the former OECD Chief Economist and CR critic; and Hermes Investment Committee Chairman: David Pitt-Watson, it appeared that some refinement of the areas of disagreement on CR, might be possible.

Specifically, although there might be continuing argument about the precise terminology, activities for which there was a business case could be broadly accepted. Instead, the disagreement focussed more on why, and in what circumstances, companies might have additional responsibilities. This paper is an initial attempt to answer this. Like all the Occasional Papers that the Doughty Centre plans to produce, this is designed to inform and provoke further debate and inquiry.

Should companies try to do good things?

When it comes to trying to address the great issues of our time: energy, global warming, biodiversity losses, water scarcity, poverty, illiteracy, human rights – all wrapped up in the concept of 'Sustainable Development' – businesses are sometimes part of the problem but also, by virtue of the huge role they play in our lives, they must be part of any lasting solution. Effective action will mostly be in places where companies directly operate but for some, particularly large trans-national companies, action may be on a global scale.

There is probably no such thing as a wholly good or bad company. All companies do good things and bad things, often at the same time, as summarised in Table 1.

As David Vogel² has argued:

"People are rarely consistent in their ethical behaviours, as numerous psychological studies have shown. An individual can cheat on his spouse and file an honest income tax return, or be a model employee and an irresponsible parent... So if it is difficult to judge the overall ethics of an individual, it is certainly more so in the case of complex business organizations. Few firms widely regarded as socially responsible consistently exhibit ethical behaviors, while even the most criticized are not without virtues."³

² David Vogel teaches business ethics at UC Berkeley's Haas School of Business and is the author of "The Market for Virtue: The Potential and Limits of Corporate Social Responsibility." 2005 – Brookings Institute

³ Vogel, David February 13, 2007 "When do 'good' firms go 'bad'? Ranking corporations by ethics is popular, but telling the good guys from the bad is not clear-cut." *Los Angeles Times*

TABLE 1

Good things	Bad things
<ul style="list-style-type: none"> • <u>Valued product/service</u> • <u>Income & training for employees</u> • <u>Profit for investors</u> • <u>Taxes for public services</u> • <u>Positive impact on community</u> • <u>Donations to good causes?</u> • <i>Leadership on sustainability</i> • <i>Leadership on ethical business</i> • <i>Leadership on positive human rights impact</i> 	<ul style="list-style-type: none"> • <u>Harmful product/service</u> • <u>Exploitation of consumers</u> • <u>Exploitation of employees (poor health & safety and working conditions)</u> • <u>Monopolistic profits</u> • <u>Excessive pay gap between top & bottom</u> • <u>Negative impact on community</u> • <i>Unpaid for environmental costs</i> • <i>Direct abuse of human rights</i> • <i>Complicity in human rights abuse by others</i>

Explaining table 1

The underlined 'good things' make up a large part of the reason why companies make such an important contribution to our material well-being. That this positive contribution is less well appreciated in Europe, certainly than it is in the USA, is a reputation issue that business in Europe should collectively address. The underlined 'bad things' are essentially the flip side of the 'good things'. In a well regulated system, it would be hoped that they would largely be prevented. However, even in the supposedly best regulated countries, it would be easy to cite instances of bad practice under each bullet point.

Donations to good causes is questioned as a 'good thing' because the dominance of the corporate philanthropy tradition in a number of countries has for too long given this pre-eminence in the popular understanding of corporate social responsibility (CSR). Where corporate philanthropy is culturally expected or where it is, in effect, a contribution to a company's community relations and good reputation generally, it is fine. Where it is little more than giving away shareholder's money to enhance the personal social status of company directors, it is clearly a bad thing. In any case the donations budget of even the most 'generous' company pales into insignificance compared to the impact on society, both good and bad, of the company's mainstream operations. It is how that impact is understood and managed which is the way in which the concept of corporate responsibility is increasingly understood. A company cannot claim to be responsible because it supports environmental projects, if it is an inveterate polluter; or claim to be a responsible business because it supports local schools if it neglects its own staff training and development needs. It cannot say it is responsible because it supports HIV/AIDS charities if it discriminates against a member of its own staff when they become HIV positive.

The 'good things' in italics are the frontier questions in public issue governance areas, in which – it is argued in this paper – companies, especially large ones, are increasingly being involved and being expected to play a positive part. The 'bad things' in italics are, again, the flip side of the 'good things' with the additional and highly contentious issue of the extent to which a company is

complicit in the human rights abuses of third parties they are dealing with, such as governments, suppliers and contractors.

The case for and against CR

The fundamental question is, and this is the essence of the debate over corporate responsibility, should the governance of good and bad things companies do, be left to market forces and state regulation; or should companies deliberately set out to do good things beyond the minimum required to pursue their medium term financial targets? Some of the arguments which have been advanced for and against Corporate Responsibility are set out in Table 2.

TABLE 2

Summary case against CR	Summary case for CR
<ul style="list-style-type: none"> • Doing good is either an ingredient of and/or a by-product of pursuit of profits • Companies are not public services • Case for CR is remake of discredited old case for public enterprise • Governments' job to look after public interest issues • CR is an inadequate substitute for government regulation • Companies have no legitimacy to interfere in public policy issues • Distraction of management from main value-adding tasks • Well-meaning but ignorant or misguided social intervention may actually destroy value 	<ul style="list-style-type: none"> • Markets need regulation • Business needs ethical values e.g. 'do as you would be done by' • These issues traditionally dealt with by national governments & established social norms and pressures • World has changed since 1989 with the collapse of the Communist regimes of eastern and central Europe which ushered in a new era of globalisation • World struggling to govern itself • Radical changes in state of governance • Regulations often weak & un-enforced • Therefore companies obliged to take on this new, if uncomfortable, CR role.

Criticism of CR comes from both the political 'Left', which wants more government regulation and from the 'Right' which favours the free market with as little regulation as possible. Critics from the 'Left' see CR as a totally inadequate substitute for enforceable regulation⁴. They tend to regard CR as a deliberate invention by the business sector to promote self-governance of corporate environmental and social impact issues; and as a way of fending off proper government regulations. In fact, this paper asserts, CR strategies and practices have largely developed as a result of a governance deficit. *De jure* regulation is often weak and un-enforced. Leading company CR practices have been partly self-generated in the light of company operational experience and

⁴ See, for example: Korten, David 1996 *When corporations rule the world* Berrett-Koehler

partly in response to civil society pressure and increasing expectations on company performance in these areas. This argument is developed further in the 'rules of the game' section below.

Critics of CR from the 'Right' regard CR as an unhelpful and costly distraction from the main role of business. They are not suggesting that companies should behave irresponsibly or unethically. Their main point is that doing good is either an ingredient of, or a by-product of, pursuit of profits, not an objective in its own right. *"It is not from the benevolence of the butcher, the brewer, or the baker that we expect our dinner, but from their regard to their own interest."* (Adam Smith)⁵ Self-interested business will naturally seek to minimise avoidable costs such as energy usage and waste disposal, and will also pay due regard to ethical practices, stakeholder interests and wider social impacts, including human rights, in so far as they impact on the company's reputation and licence to operate. Milton Friedman himself recognised this in arguing 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"*⁶, which is to say, engages in open and free competition without deception or fraud. Friedman recognised that "rules of the game" could include the prevailing ethical standard. The anti-CR case⁷ is that by introducing environmental and social objectives beyond those required by the nature of a company's business model and the rules of the game, serious issues of loss of management focus, incompetence and legitimacy need to be addressed. To quote Adam Smith again *"Virtue is more to be feared than vice, because its excesses are not subject to the regulation of conscience."* For conscience also read reputation and brand value.

Those who argue against CR, it seems, basically accept the so-called 'business case' for CR which is summarised in table 3 below⁸.

TABLE 3

<p>The Business Case for CR – it helps</p> <ul style="list-style-type: none"> • Risk management • Reputation management • Staff recruitment, retention and motivation • Market growth • Product or service differentiation • New business opportunities • Cost savings • Access to and lower cost of capital
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In effect, free market critics of CR regard activities for which there is seen to be a business case, as part of doing normal business in pursuit of profits. What

⁵ Smith, Adam, 1776 *Wealth of Nations* book 2 chapter 1

⁶ Milton Friedman 'Capitalism and Freedom' 1962

⁷ See for example:– Henderson, David – *Misguided Virtue* Institute for Economic Affairs:
<http://www.iea.org.uk/files/upld-release5pdf?.pdf> – accessed December 20th 2007

⁸ Sourced from: Grayson, David and Hodges, Adrian 2004 *Corporate Social Opportunity* Greenleaf; Corporate Sustainability - An Investor Perspective The Mays Report – Australia 2004; Arthur D. Little "The Business Case" (2002) Business in the Community

they argue against is the idea that companies should be expected deliberately to set out to do good things beyond activities in pursuit of profits. In other words beyond the minimum required to maximise shareholder value⁹, which is the commonly asserted business objective. That minimum may be well below what environmental and human rights advocates demand but – critics of CR argue – it is up to those advocates to convince national governments and, in turn, international governance agencies to make the necessary regulatory changes. It is not, they argue, the job of companies to get involved in these issues. Indeed, the argument goes further to assert that intervention by companies into issues which are the proper preserve of governments actually lets the existing governments, however weak and corrupt, off the hook and does nothing to encourage them to start doing what they should be doing¹⁰. In other words it prolongs indefinitely, weak governance.

Those who argue for CR need to take these points very seriously. It is possible, even likely, that some of the basic underlined 'good things' in Table 1 above, *could* be reduced by insistence that companies take on board environmental and social objectives beyond that required by their business model – at least in the short to medium term. The pro-CR lobby needs to be able to demonstrate four things:

- First, that the traditional time scale of the market is too short given the nature of sustainability issues companies are increasingly facing.
- Secondly, that there has been a significant "power-shift" towards markets and international businesses since the collapse of the Communist regimes and the privatisation and liberalisation of many markets.
- Thirdly, that in consequence, the "rules of the game" governing the private enterprise impacts on public interest issues (or "externalities" as economists call them), are neither adequate for today's conditions nor in any case being enforced.
- Fourthly, that involvement by companies in the *de facto* governance of such issues, including establishing voluntary guidelines and principles, *can* be done in a way that leads inexorably to the establishment of more legitimate, *de jure* governance processes.

1. Timescale

The Brundtland Commission, formally known as the UN-convened World Commission on Environment and Development¹¹ in 1987 defined Sustainable Development as

'Development which meets the needs of the present without compromising the abilities of future generations to meet their own needs'.

⁹ "What matters is not investor holding periods but rather the market's valuation horizon—the number of years of expected cash flows required to justify the stock price. While investors may focus unduly on near-term goals and hold shares for a relatively short time, stock prices reflect the market's long view. Studies suggest that it takes more than ten years of value-creating cash flows to justify the stock prices of most companies." Rappaport, Alfred – *Ten ways to create shareholder value* – Harvard Business Review Online – accessed December 20th 2007

¹⁰ This appears to be the criticism of CR made by Reich, Robert in *Supercapitalism* – 2007 Borzoi Books; also Bakan, Joel 2005 *The Corporation* Robinson Publishing

¹¹ World Commission on Environment and Development 1987. *Our Common Future* - Oxford University Press

The market is not able to take the needs of future generations into account unless consumers and investors demand it through their market choices or rule makers enforce it. It has been estimated that a tax of \$85 per ton of carbon emitted would provide the right signal for the market to bring about the necessary investment and spending adjustments to address Climate Change¹². (See research by Dr Chris Hope of the Judge Institute in Cambridge, using a model of climate change which assesses the costs and benefits of various mitigation and adaptation strategies. However, there is still much argument about the appropriate rate of time discount used in the calculations.)

Green consumers and ethical investors are increasing in numbers but are still far too small a proportion of the whole to have a major impact. Rule-makers globally are on the whole, so far, either unable or unwilling to do what would be required. Like the political horizons of many rule-makers, many would argue that markets are essentially short to medium term and financial returns are geared to that time-scale. Unless business leaders can be convinced that the long term sustainability of their companies is at stake and, in turn, can persuade investors to take a longer view, this will not change unless or until some kind of catastrophe changes the paradigm.

2. Power-shift – New global realities

It is the traditional and legitimate role of governments to look after the public interest. Economists have always accepted that private companies create public value from which they receive no revenue, and public cost for which they do not pay. These are called externalities and it is entirely reasonable for governments to regulate, tax and/or subsidise companies to take account of them. Laws concerning restraint of trade, monopoly, labour rights, pollution, building regulations are all examples of how governments have traditionally tried to regulate the market to operate in the wider public interest. The main case for the pro-CR lobby rests on three assertions about the state of governance: firstly, that in a global, connected society, governments alone are no longer able effectively to look after the public interest in the way just described; secondly, that the lack of effective governance of global issues is becoming more apparent and urgent; thirdly, that companies do business in many weak and failed states where governance is both lacking and often corrupt.

Post 1989, and the implosion of the Communist regimes of eastern and central Europe, globalisation has taken a new form. It has created an almost unbounded presumption for the free market. The Information and Communications Technology explosion has enabled unprecedented global connectivity. Business is now 24/7. Flows of finance, information and trade take little heed of state boundaries. This has created international competitiveness pressures which have much reduced governments' ability to regulate, tax and provide public welfare. In addition, problems of a global dimension, such as climate change, ecosystem losses, water deficits, poverty issues, health issues, human rights and corruption, are growing with a speed

¹² Comments by Dr Chris Hope – European Academy for Business in Society Annual Colloquium September 2007 – noted by authors – See also: www.eabis.org/csrplatform/colloquium/2007/2007proceedings/ClimateChangeResourceCentre/

and potential scale of impact greater than ever before, exacerbated by rapid population growth. So, not only have national governments lost autonomous power, the implications of the long-standing deficit in global governance are even more pressing. Power has shifted, particularly towards large, transnational companies – and especially now to a new generation of global enterprises¹³.

Recognition and acceptance of this power shift is critical to the case for CR¹⁴. If there were a world of internationally collaborating, national governments holding corporations to account through strong internal regulations backed by strong international law and enforcement institutions, then CR would be far less important. It could perhaps revert to how most companies interpreted CSR prior to 1989, which was mainly a discretionary approach to behaving ethically and investing in community relations and corporate philanthropy. It would not require companies to take a pro-active role in addressing public interest issues unless it was specifically in the immediate business interests of the company to do so. However, such an effective regulatory environment is highly unlikely in the foreseeable future. The 'rules of the game' will remain in *de jure* terms weak and un-enforced. Whether the public or the companies themselves like it or not, companies will be involved for many years to come in decision-making which greatly affects the public interest and which governments alone will fail adequately to address. In other words, companies are inescapably involved in public policy issues.

This is giving many CEOs, keen to maximise shareholder value, an increasing number of difficult decisions, like those described by Chris Marsden in the European Business Forum's ethics debate 'When in Rome ...?'

*"You have been approached to join a working group of business leaders to produce a report on global warming. One of your colleague directors has come up with a proposal to relocate one of your plants to India to benefit from cheaper labour and lower health and safety regulations. Your Africa area manager is pressing you to sign a lucrative contract which entails a 30% facilitation fee, most of which you know will end up in the pocket of the trade minister. You have a strong equal opportunities policy in Europe, based on EU standards, but your business development in the Middle East depends on not appointing women to key positions. You are being offered excellent terms by a South American government for a major investment opportunity but you know this is strongly opposed by the local indigenous community. You are already facing criticism in the press for using the security forces of another South American country to defend your assets from attack by insurgent groups. You source manufactured materials from the Far East and suspect these factories use child labour. These are issues that are properly the job of governments to resolve and set rules for, but you know that they are neither individually nor collectively likely to do so."*¹⁵

¹³ For a good discussion of the nature of the new global as opposed to multinational businesses see article by the President and CEO of IBM – [Samuel J. Palmisano](#) – 2006. *The Globally Integrated Enterprise* – Foreign Affairs, [May/June 2006](#);

¹⁴ For the implications for business: see the conclusions of a group of international business leaders: "Challenges and Choices: Tomorrow's Global Company Inquiry 2007 – Centre for Tomorrow's Company [www.tomorrowcompany.com/global/default.aspx](#) accessed December 20th 2007

¹⁵ Marsden, Chris 2007 "When in Rome..?" - European Business Forum ,Issue 31, Winter 2007, page 20.

3. New Rules of the game

These power-shifts mean in practice that companies are involved now in a range of public issue governance decisions exemplified by those summarised in Table 4. This means that Milton Friedman's "rules of the game" have changed. These new rules of the game are a hybrid of laws and regulations applied extra-territorially, heightened societal expectations, and ethical/moral sentiment and judgement. In effect, the business case just got extended.

TABLE 4

Examples of public issue governance decisions faced by companies:

- Taking a precautionary approach to global warming
- Whether or not to develop the use of genetically moderated crops
- Marketing life-saving drugs in poor countries at lower prices
- Whether or not to pursue money laundering
- Doing pre-investment environmental and social impact assessment
- How to manage conflicting interests of a national government versus those of an indigenous community where a company is operating
- Whether or not to pursue global policy on human rights or accept local practices
- Which human rights to prioritise when faced with an "on-the-ground" dilemma
- Whether or not to raise "awkward" issues with host government
- How to manage relationship with state security forces during internal conflict
- To go in, stay in, or pull out of a 'rogue state'

When a leading energy company decides that the evidence of global warming is too great to ignore and publicly adopts policies to restrict its greenhouse gas emissions and pursue alternative energy sources, this has a public impact. The impact, for instance, in terms of opinion-leadership, may be far wider than just on the company itself. A decision to fund research that will try to obscure the global warming debate is similarly an intervention in public issue governance. When an agro-chemical company decides to develop GM (genetically-modified) technology without due regard to public opinion, it is capable of creating a climate of anti-GM opinion that sets back by many years a development which may have an answer to world food shortages. Pharmaceutical companies have the capability of providing many life-saving drugs to poor countries and increasingly are expected to be more imaginative in looking for alternative funding and delivery strategies. Banks, most of which are now international in reach, have the capability of tracking money-laundering and other money flows of dubious legality, which could considerably reduce the misappropriation of public funds. All these actual cases illustrate the new global realities for business.

In a well-regulated country, when a company wants to undertake a major investment project, it is subject to planning regulations and probably a public enquiry which has the power to make adjustments to the plans in the face of public opposition; or in an extreme case to stop the development altogether. In many parts of the world this simply does not happen, sometimes because of

poor regulatory processes and sometimes because those in power in government want the revenues and are not interested in the external costs of the project on the local communities affected. In these cases companies on their own initiative are increasingly expected by non-governmental organisations (NGOs) and public opinion more widely, to undertake both pre-investment and on-going environmental and social impact analyses in full collaboration with affected stakeholders. In this way, plan modifications and compensation can be openly negotiated and may even (though rarely) lead to a project being abandoned entirely. This, again, is active involvement by companies in public interest issue governance.

Companies are clearly expected to obey the laws of the country in which they operate. But what should they do if those laws encourage ethical, environmental and/or human rights standards below those required by international law or principles established by voluntary groupings of companies, NGOs and government representatives in other parts of the world? In such circumstances companies may stand firm with their principles, for instance with a 'No Bribes' policy. They may decide to give priority to benefits they can bring through creating jobs and livelihoods, while deferring concerns over local denial of equal opportunity rights and labour conditions. They may decide to raise with government ministers, issues of human rights abuses, such as use of forced labour or displacement of people. Both the Voluntary Principles on Security and Human Rights¹⁶ and the Extractive Industry Transparency Initiative¹⁷ are examples of voluntary undertakings by global companies to maintain internationally agreed standards of behaviour when operating in weak governance zones, and to raise issues of concern directly with relevant government authorities. In "worst case" scenarios, companies may be expected to disinvest in countries with pariah governments. This is, of course, a much more dilemma-strewn decision than whether to invest in the first place.

These and many more examples are decisions which companies cannot avoid. Clearly, each company needs to be very careful to understand and work within its sphere of influence and the materiality to its business of the issue in question. But companies do have the power to make a difference for good or bad. These are, in effect, decisions of governance over public policy issues. To step aside and do nothing is as much a decision with implications for the issue in question, as to get directly involved. In a well-governed world the 'leave it to market forces within the rules of the game' case would be persuasive. But the world is not well-governed and shows no signs of being so in the foreseeable future. The case for active CR by companies to contribute to filling the *de facto* governance gap at the international level and in states with weak or despotic government, is inescapable. However, it is a very imperfect and – ideally – a transitory scenario. This is not something that companies are designed for, or are particularly good at. Companies are not natural guardians of the public interest. Their legitimacy is only that of being in situations where there is weak or ineffective governance, and where they have the power to

¹⁶ The Voluntary Principles on Security & Human Rights - www.voluntaryprinciples.org - accessed December 20th 2007

¹⁷ Extractive Industries Transparency Initiative www.eitransparency.org - accessed December 20th 2007

make a positive difference to an issue as, for instance, in the cases of the Extractive Industries Transparency Initiative mentioned above.

4. From *de facto* to *de jure* Governance?

The final issue is how company engagement in these issues can eventually translate into the establishment of more legitimate, *de jure* governance processes, rather than seeming to relieve governments of their proper responsibilities and prolonging a series of “second best” outcomes. First, it should be said that second best or less than perfect outcomes are often preferable to the *status quo* in a world that is struggling to govern itself, making *de facto* governance processes work as well as possible would seem to be preferable to waiting for more formal, *de jure* governance, which may take a long time to evolve. To encourage the latter requires companies to approach their involvement as transparently as possible and work with all relevant stakeholders, including governments – so easily said but so hard to do, with competing interests, strong sensitivities and limited resources.

“Tomorrow’s Global Company: Challenges and Choices” suggests that one key role now for Global Companies is setting standards – these may be at the level of the individual firm; voluntary, industry-wide agreements; or the fore-runner of mandatory national or international standards¹⁸. Professor Atle Midttun from the Norwegian School of Management has suggested that individual companies adopting corporate responsibility may be self-regulators. Midttun further argues that where a group of companies together adopt higher standards of ethical, environmental and / or social performance, they are co-regulating. Interestingly, Midttun is not a political scientist – he teaches innovation at the Norwegian School of Management in Oslo.

Midttun further suggests that putting some kind of democratic framework around these voluntary company commitments may also be one of the ways of addressing some of the current criticisms of corporate responsibility as being either undemocratic or anti-competitive¹⁹. The Extractive Industries Transparency Initiative is a good example of this process. The EITI began after BP tried and failed to publicise the royalty payments it was making to the Angolan Government. With the help of the British Government and subsequently of several other governments, BP has persuaded other energy companies to increase transparency and publish what they pay. Several governments have now endorsed and put their weight behind the EITI. Similarly, by helping to fund the secretariat of the Carbon Disclosure Project, governments are endorsing this voluntary initiative to get the world’s largest companies to state whether they have carbon reduction strategies in place. Individual governments could have passed laws requiring companies in their jurisdictions to answer questions about carbon reduction strategies. In practice, the Carbon Disclosure Project – endorsed by more than 300 of the

¹⁸ “Challenges and Choices: Tomorrow’s Global Company Inquiry 2007 Final Report from Tomorrow’s Global Company Inquiry, London, June 2007 – www.tomorrowcompany.com

¹⁹ Prof Atle Midttun – Norwegian School of Management, Oslo – 2007 – European Academy for Business in Society Annual Colloquium September 2007 - noted by authors
<http://www.eabis.org/csrplatform/colloquium/2007/2007proceedings/SecondPlenary/>

world's largest institutional investors, representing more than \$41 trillion of funds – probably has more sway than most governments²⁰.

With many national governments apparently unwilling to help lead the drive for better global governance, increasing numbers of people are looking to non-governmental or civil society organisations to represent particular interests, such as the environment and human rights. NGOs, with varying degrees of popular legitimacy, act as watchdogs and whistle-blowers about corporate behaviour. They have become a form of countervailing power to that wielded by large companies, often commanding greater public trust than companies particularly in Europe²¹, although with considerably less financial resources and often less formal rights in existing law.

By 2000 there were more than 37,000 International NGOs and over 20,000 transnational NGO networks²². Within this civil society, there is considerable difference of opinion as to whether to pursue undiluted oppositional tactics to what companies are doing or whether to engage in constructive dialogue and even partnership. Indeed more radical groups, like London Rising Tide²³ openly criticise the likes of WWF and Greenpeace for taking part in joint conferences with leading oil and mining companies, for selling out to big business and thus contributing to what the radicals call the plague of 'greenwash'. It is interesting to note that only 10 years ago it was Greenpeace which first recognised the emerging power of civil society to pressurise companies independently of government action, in its high profile action against Shell over the disposal of the Brent Spar oil storage unit in the North Atlantic. Since then, the campaigning environmental organisation, like several other leading NGOs, has grown as a 'political' institution and has been drawn into more of a problem-solving role alongside its whistle-blowing one. It has come to take a more pragmatic view that for all their failings, companies do have a huge role to play in solving the world's major problems. They have to be part of the solutions not just a cause of the problems, and they need all the help they can be given, to do it well²⁴.

Table 5 suggests one model of the stages that a contentious issue affecting business, may pass through from the perspective of NGOs campaigning on the issue.

²⁰ see www.cdproject.net – accessed Dec 21st 2007

²¹ see Richard Edelman Address to Ethical Corporation Magazine conference, New York, 3 October 2002 "ReEvolution of Business: A Mandala for the 21st Century" www.ethicalcorp.com/content.asp?ContentID=346

²² (see [UNDP Human Development Report 2002 - Chapter 5: Deepening democracy at the global level](#)).

²³ www.londonrisingtide.org.uk accessed December 20th 2007

²⁴ For an early articulation of such a constructive NGO role see Schwartz, Peter and Gibb, Blair (1999) 'When Good Companies do bad things Responsibility and Risk in an Age of Globalization', page 135, .John Wiley & Sons

TABLE 5²⁵

1. An activist NGO floats an issue as a problem
2. NGOs, usually in coalition, initiate a campaign to which public opinion responds
3. With enough public response, governmental or intergovernmental bodies become involved, and NGOs participate in drafting new laws, regulations or codes
4. NGOs become active monitors of legal/regulatory/code compliance
5. NGOs become resources to corporations in future policy decisions.

The BP and Amnesty International engagement (Box 1) over the human rights issues regarding the Baku-Tblisi-Ceyhan ('BTC') pipeline, which ultimately contributed to the International Finance Corporation's (IFC) review of its project lending rules, is one example of how these new *de facto* governance processes can translate into more formal rules of the game²⁶.

BOX 1 Baku-Tblisi-Ceyhan ('BTC') pipeline case-study

Following publication by BP of the company's Host Government Agreement (HGA) with Turkey in 2003, Amnesty International expressed concerns that the agreement was most likely to lead to denial of the human rights of those living in the area of the pipeline. Amnesty argued that the HGA could have a 'chilling effect' on the Turkish government's willingness to enforce their human rights, labour rights, and environmental obligations, which it had agreed under international treaties²⁷. Amnesty warned that the land acquisition could have the effect of resettling the 30,000 people who would be forced to give up their land rights to make way for the pipeline; there could be inadequate enforcement of health and safety legislation to protect workers and local people; and there could be a serious risk to the human rights of any individuals who protested against the pipeline. Amnesty expressed particular concern about the HGA clause indicating that host countries are liable for any disruption to the economic equilibrium of the project. It feared that this would create a disincentive for the Turkish government to protect human rights because it had agreed to pay compensation to the BTC consortium if the pipeline construction or operation were disturbed.

BP listened to Amnesty's concerns but responded by asserting that the Company's well known strong human rights policy, based on the Universal Declaration of Human Rights, meant that it could be trusted not to deny human rights associated with the construction and operating of the pipeline. Amnesty was not persuaded, pointing to other failings BP had experienced and suggesting that when times get tough the lawyers tend to win the argument. The impasse was finally resolved when Amnesty called a public meeting to launch the publication of its report 'Human Rights on the Line'²⁸, which demonstrated its concerns in detail. A week

²⁵ *ibid*

²⁶ The BTC Pipeline Case Study, Global Compact Learning Forum
http://www.unglobalcompact.org/docs/communication_on_progress/4.2/4.2.4/boa_bp.pdf accessed December 20th 2007

²⁷ <http://www.ilo.org/public/english/about/history.htm> ; <http://www.un.org/Overview/rights.html>

²⁸ Human Rights on the Line: Amnesty International, May 2003
<http://www.amnestyusa.org/business/humanrightsontheline.pdf> accessed December 20th 2007

later BP asked Amnesty for further talks. The Company now accepted Amnesty's conclusions and after lengthy negotiations between lawyers representing the two organisations a compromise settlement was reached in which a Deed Poll (a legally binding contract designed to protect the rights of the Turkish government to promote and regulate human rights and environmental issues) was drafted and then signed by the BTC Project. Subsequent to this agreement, BP and Amnesty have had discussions with the IFC, a subsidiary of the World Bank, which provided loans to the BTC project. This has contributed to the IFC's review of its lending conditions to take more account of human rights issues.

CONCLUSIONS

What is the ultimate governance vision? Is it a world of internationally collaborating, representative national governments holding corporations to account through strong internal regulations backed by strong international law and enforcement institutions? Can that realistically be achieved in time before irreversible and calamitous climate and other environmental and social degradation takes place? If this theoretical “ideal” public governance state were to occur, the case for CR might revert to that on which there does seem to be a consensus: that is, responsible behaviour by companies should rest on a business case backed up by strong ethical values and enforced rules of the game. In the meantime, given the likelihood of a lasting deficit of enforced rules of the game, the case for CR, i.e. for companies being expected to try deliberately to do good things beyond the minimum required to pursue their immediate financial targets, is a strong one. As that expectation is increasingly being backed up by NGO action, usually targeted at the big trans-national companies and brands, responsible involvement in public issues is becoming an unavoidable part of the new rules of the game. In time, perhaps, these companies will come to recognise that their interest lies in a creating a level playing field on which to compete.

All those involved in this pragmatic, *de facto* governance process should see this – at least theoretically – as an ultimately transitory, if long term, phenomenon and work together to assist the development of better *de jure* governance processes. It must be in the long term interest of leading companies and the associations which represent them, to work tirelessly towards the creation of more effective regulations by legitimate governments so that they can compete fairly with other companies which now take a free ride on CR matters. That implies that leading companies and their associations should be actively lobbying governments for better regulation, not less. If and when the governance of company impacts on environmental and social issues is firmly brought within the rules of the game, then CR can perhaps return to being largely discretionary – but that time is a long way off. It remains an open question, in the face of the greatly increased complexity of the issues facing global society, whether governments alone, however well-organised, professional and far-seeing they are, can even theoretically, be able to solve the major environmental and societal issues on their own.

THE AUTHORS

Chris Marsden is Chair of Trustees of the Business and Human Rights Resource Centre, Board member of the European Academy of Business in Society, Visiting Professor at the International School of Management, Ecole National des Ponts et Chaussées and Associate of the Doughty Centre for Corporate Responsibility at Cranfield University. He was Chair of Amnesty International (UK) Business Group from 2001 to 2007 and was formerly Head of Community Affairs for BP.

David Grayson is Chair of Corporate Responsibility and Director of the Doughty Centre for Corporate Responsibility. He chairs the UK Small Business Consortium. He is a visiting Senior Fellow at the CSR Initiative at the Kennedy School of Government, Harvard. He is a former Managing Director of Business in the Community. He has chaired or served on the board of several UK Government agencies and advised several international agencies.

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