

Unpacking the Reforms in Europe and UK Relating to Mandatory Disclosure in Corporate Social Responsibility: Instituting a Hybrid Governance Model to Change Corporate Behaviour?

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Abstract and Introduction

Corporate social responsibility is a key point of intersection at the junctures of business, society and government.¹ It has first been conceived of as voluntary or self-regulatory measures that address, at least in part, complex issues that entail from corporate activity, whether they relate to direct or indirect forms of externalities or indeed the provision of proactive 'good' for social causes and objectives. Global corporate activities are increasingly related to the provision of global public or collective goods,² such provision no longer confined to public sector actors. This is arguably because the existence of the needs for global public goods is due to the externality-creating actions on the part of corporations that consume planetary resources and often fail to internalise social cost associated with their activities. Corporations suffer from a collective action problem in refraining from creating such externalities (as their competitors may persist in doing so) as well as redressing them- both are phenomena of the tragedy of the commons. Global public goods include environmental protection, sustainability in the use of planetary resources, adequate standards and protection of certain humanity conditions such as human rights, labour rights and communities, development, addressing the sub-optimal institutions in political economy (such as tax havens and corruption), and social transformations (such as consumerism).³

Voluntary corporate responsibility may not be able to keep pace with the intensity and range of social demands, not to mention that the incentives that drive corporations often diverge from social expectations. The needs for these global public goods arise in a polycentric space of actors and stakeholders including states, international organisations and other public and private sector stakeholders.⁴ States and law-makers are not necessarily able to command this space⁵ as the

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¹ Jeremy Moon, Nahee Kang and Jean-Pascal Gond, 'Corporate Social Responsibility and Government' in David Coen et al (eds), *The Oxford Handbook of Business and Government* (Oxford: OUP 2010) at ch22; George A Steiner and John F Steiner, *Business, Government and Society* (7th ed, McGraw-Hill, 1994) for an overview in chapter 1.

² Inge Kaul, 'Rethinking Public Goods and Global Public Goods' in Inge Kaul (ed), *Reflexive Governance for Global Public Goods* (Cambridge: MIT Press 2012).

³ For a comprehensive list of general literature on aspects of corporate social responsibility, please see Appendix 2.

⁴ A taxonomy of governance actions is provided in chapter 4; 21-25, John Braithwaite and Peter Drahos, *Global Business Regulation* (Oxford: OUP 2000); also broadly discussed in Larry Catá Backer, 'Theorizing Regulatory Governance Within its Ecology: The Structure of Management in an Age of Globalization' (2016) at <https://ssrn.com/abstract=2783018>; Peer Zumbansen, 'The Conundrum of Corporate Social Responsibility: Reflections on the Changing Nature of Firms and States' (2006) at <http://ssrn.com/abstract=885373>.

⁵ Contemporary literature is generally acknowledging the rise of governance, which is a pluralistic concept that explains how spaces for problem solving and dialogue are populated by many actors, and not monopolised by

transnational context for global multi-national corporations and the complexity of issues that affect a wide range of stakeholders increasingly elude state-based authority and mechanisms.

Polycentric governance is an important paradigm *du jour* for analysing these issues. The importance of polycentric governance is reflected in the development of reflexive means of governance in law and policy to be discussed shortly. However, commentators increasingly observe a 'juridification' of corporate social responsibility and the extension of regulation and legalisation (in various forms).⁶ This is largely due to increasing pressure for change in corporate behaviour over years of slow achievements in the voluntary efforts led by the corporate sector. A 'new' regulatory technique, which is found in the EU Non-financial Reporting Directive 2014 implemented in the UK Companies Act 2006, and to a lesser extent in the UK's Modern Slavery Act 2015 seems poised to draw together the polycentric forces of governance in a new way and yet leverage upon the power of state-backed regulation to achieve changes to corporate behaviour.⁷

We suggest that such a new regulatory technique brings about new opportunities for corporate behaviour to be shaped by social input. This can incrementally result in cultural and behavioural change at corporations. Although this technique may appear 'weak' as corporate law is not significantly reformed, intrusive or 'command'-forms of hard law need not be superior. What matters is whether behavioural change can be secured. This article makes a positive case for the social implications of the new mandatory disclosure obligation, although we acknowledge that this is not a silver bullet. The article does not take the view that other forms of hard law reforms such as in relation to corporate objective, directors' duties etc⁸ are unnecessary. The complementarity between the case put forward in this article and other reform options is a subject for another discussion.

In this article, Section A will discuss briefly the context for 'juridification' or 'legalisation' of issues of corporate social responsibility. Section B discusses the provisions in the EU Non-financial Disclosure Directive (and the equivalent in the UK Companies Act) and how procedural regulation for corporations is introduced via a form of mandatory disclosure. Section C discusses the UK's Modern Slavery Act regime which employs less legalisation and compares this to the non-financial disclosure regime. Section D draws together a few broad critical reflections and concludes.

regulators or governments. See Julia Black, 'Critical Reflections on Regulation' (2002) 27 *Australian Journal of Legal Philosophy* 1; Stephen P Osborne (ed), *The New Public Governance?: Emerging Perspectives on the Theory and Practice of Public Governance* (Oxford: Routledge, 2009).

⁶ The term 'juridification' is used in Karin Buhmann, 'Reflexive Regulation of CSR to Promote Sustainability: Understanding EU Public-Private Regulation on CSR Through the Case of Human Rights' (2010) at <http://ssrn.com/abstract=1712801>. Also see Reinhard Steurer, 'The Role of Governments in Corporate Social Responsibility: Characterising Public Policies on CSR in Europe' (2010) 43 *Policy Sciences* 49-72 reflecting on increasing political interest and government involvement in CSR; Jette Knudsen, 'Bringing the State Back in? US and UK Government Regulation of Corporate Social Responsibility (CSR) in International Business' (2014) at <http://ssrn.com/abstract=2541002> on the increasing social appetite for regulatory governance in CSR issues.

⁷ Sections B and C.

⁸ See excellent panoply of discussion in the *European Company Law*, Issue 11(2) (2014) featuring a special issue on sustainable companies.

A. Legalising or Juridifying Corporate Social Responsibility

Corporate social responsibility encompasses business, legal and beyond-legal dimensions such as ethics and citizenship.⁹ A responsible corporation is not only legally compliant, there is an expectation that responsibility extends beyond the legal dimension into the realm of being ‘good’, ‘ethical’ or ‘moral’.¹⁰ It may be argued that such ‘spirited responsibility’ lies in the domain of private preferences based on values and mission, and cannot be the subject of regulated behaviour.

Drawing the line between what is *regulable* conduct and otherwise is a difficult one. This is because the lack of regulation of conduct is not always due to its inherent unregulability. The lack of regulation could be a result of lack of perceived necessity or political will. Indeed corporations could engage in voluntary conduct in order to prevent the regulation of an issue area. However, persistent gaps between social expectations and corporate social performance could in time culminate in some form of regulatory leadership, i.e what may be thought of as ‘good behaviour’ may become what is legally required conduct.

The increasing juridification of corporate social responsibility is arguably a reflection of that development. The following confluence of factors are in our view important:

- (a) Firm and market limitations in meeting social expectations, which have persisted over decades of corporate scandals;
- (b) Incremental and stealthy developments in corporate regulation which have over the years established the legitimacy of ‘regulatory capitalism’;¹¹ and
- (c) A surge in international policy and social appetite for legalisation and regulation in the wake of the global financial crisis 2007-9.

Firm and Market Limitations

In the 1950s-70s, the rhetoric surrounding corporate responsibility was anchored in ethical and citizenship consciousness, bound up in the firm’s conception of its public-facing self and socially-anchored personhood.¹² The inward-looking nature of the firm has developed much more recently,¹³

⁹ Archie B Carroll, ‘Corporate Social Responsibility’ (1999) 38 *Business and Society* 268.

¹⁰ Doreen McBarnet, ‘Corporate Social Responsibility Beyond Law, Through Law, for Law’ (2009) at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=1369305.

¹¹ See David Levi-Faur, ‘The Global Diffusion of Regulatory Capitalism’ (2005) 598 *ANNALS of the Academy of Political Science* 12; John Braithwaite, *Regulatory Capitalism* (Cheltenham: Edward Elgar, 2008).

¹² Carroll (1999) above and William W Bratton, ‘The Separation of Corporate Law and Social Welfare’ (2017) *Washington and Lee Law Review*, forthcoming at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2927150.

¹³ From the 1970s, with Friedman’s focus on firm-centred business performance as central to its social responsibility, and Jensen and Meckling’s agency-based view of corporate governance, see M Jensen and W Meckling, ‘Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure’ (1976) 3 *Journal of Financial Economics* 305.

as shareholder primacy has become a governing mantra for corporate management.¹⁴ Concern for social welfare fell away from the management radar since the 1980s as privatisation, economic liberalisation and financialisation took root.¹⁵

The notion of corporate responsibility is today framed much more in alignment with the business case,¹⁶ and responsible behaviour is shaped by fears of informal reputational sanctions in the form of media or activist pressure, or consumer aversion.¹⁷ Where the business case may be weaker or more nuanced, firm-led or industry-led initiatives in corporate responsibility may be absent or less effectual.¹⁸

We raise critically the example of the Equator principles,¹⁹ developed by leading banks to ensure that their project finance decisions are in line with the social responsibility concerns of the project.²⁰ The development of such Principles may be important in preventing intrusive regulations concerning the social aspects of project finance. The Principles oblige banks to **monitor** the borrower's assessment of the social responsibility impact of the project and continuing management of such impact in consultation with stakeholders. However, the quality of monitoring undertaken by each bank, especially in the post-contractual phases, depends on the bank's own processes²¹ which are not subject to independent review. Hence, the actual outcomes achieved for stakeholders affected by project finance are not subject to independent evaluation and accountability.²²

¹⁴ The rise of shareholder primacy and its adverse impact on the wider responsibility consciousness of corporations is discussed in Iris H-Y Chiu, 'Operationalising a Stakeholder Conception in Company Law' (2017) Law and Financial Markets Review forthcoming and citations therein.

¹⁵ William W Bratton, 'The Separation of Corporate Law and Social Welfare' (2017) Washington and Lee Law Review, forthcoming at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2927150.

¹⁶ Cathie Jo Martin, 'Social Policy and Business' in David Coen et al (eds), *The Oxford Handbook of Business and Government* (Oxford: OUP 2010) at ch24.

¹⁷ Regina Kreide, 'The Obligations of Transnational Corporations in the Global Context. Normative Grounds, Real Policy, and Legitimate Governance' (2006) 4 Ethics and Economics 1 at <http://ssrn.com/abstract=1096102>; David Vogel, 'Taming Globalisation? Civil Regulation and Corporate Capitalism' in David Coen et al (eds), *The Oxford Handbook of Business and Government* (Oxford: OUP 2010) at ch20.

¹⁸ Paul Calcott, 'Mandated Self-Regulation: The Danger of Cosmetic Compliance' (2010) 38 Journal of Regulatory Economics 167-179. On the use of 'symbolic' structures to signify compliance, without meaningfully observing the spirit of legislation see: Laruen B. Edelman, 'Legal Ambiguity and Symbolic Structures: Organizational Mediation of Civil Rights Law,' (1992) 97(6) American Journal of Sociology 1531.

¹⁹ The Equator Principles (2013) at <http://www.equator-principles.com/index.php/ep3>.

²⁰ Reputational concerns are the main incentives relevant to banks that adopted the Principles, see Christopher Wright and Alexis Rwabizambuga, 'Institutional Pressures, Corporate Reputation, and Voluntary Codes of Conduct: An Examination of the Equator Principles' (2006) 111 Business and Society 89.

²¹ Patrick Haack, Dennis Schoenborn and Christopher Wickert, 'Exploring the Constitutive Conditions for a Self-Energizing Effect of CSR Standards: The Case of the "Equator Principles"' (October 2010) University of Zurich Institute of Organization and Administrative Science IOU Working Paper No 115 http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1706267, 21.

²² Critique can be found in Niamh O'Sullivan and Brendan O'Dwyer, 'Stakeholder Perspectives on a Financial Sector Legitimation Process: The Case of NGOs and the Equator Principles' (2009) 22 Accounting, Auditing & Accountability Journal 553-587; but see Bert Scholtens and Lammertjan Dam, 'Banking on the Equator. Are

Further, the relational paradigms between corporations and their various stakeholders may not culminate in sufficient pressure for corporate behavioural change. On the one hand, civil society pressures can be compelling for companies as their reputations and bottom lines can be adversely affected. For example the use of child labour by Nike's Far-Eastern suppliers exploded in the media due to civil litigation spearheaded by Mike Kasky against Nike's misrepresentations in its corporate responsibility reporting.²³ However, Wen²⁴ remarks that in a polycentric space, the governance power and capacity on the part of different constituents differ markedly, with businesses and states being relatively more powerful than consumers and civil society groups, hence skewing the nature of bottom-up initiatives. Hutchens²⁵ also argues that the governance capacity of the social sphere is a complex issue as civil society actors are not always coordinated and can fork into different directions, undermining the strength of the movement, such as in Fairtrade. Further, economic incentives remain at play, and cost concerns may deter both buyers and producers in the fair-trade movement from adopting the relevant processes and certification requirements.

Next, it may be argued that markets provide a form of governance. For example if key market players such as investors value a corporation's social responsibility profile highly, pressure can be brought to bear on corporate priorities and conduct.²⁶ Institutional investors are increasingly embracing corporate social responsibility as a key tenet for their investment decisions,²⁷ but many commentators see investors as still being focused on traditional financial returns, and do not play an active role in championing social responsibility as such.²⁸ That said, changes to investment strategies, albeit incremental, such as adhering to an Index that values social responsibility (for eg the

Banks that Adopted the Equator Principles Different from Non-Adopters?' (2007) 35 World Development 1307, but the perception of responsible conduct is measured in a more 'proxy' manner, relating to shareholder perception and existence of policies.

²³ *Kasky v Nike Inc* 45 p.3d 243 (Cal 2002).

²⁴ Shuangge Wen, 'The Cogs and Wheels of Reflexive Law ± Business Disclosure under the Modern Slavery Act' (2016) 43 Journal of Law and Society 327; W. Scheuerman, 'Reflexive Law and the Challenges of Globalisation' (2001) 9 Journal of Political Philosophy 81.

²⁵ Anna Hutchens, 'Defiance in the Social Sphere: The Complexity Of Risk Regulation In The Case Of Fair Trade' in Bettina Lange (ed), *From Economy to Society? Perspectives on Transnational Risk Regulation* (Emerald Insight 2014) at 163.

²⁶ For eg see Benjamin Richardson who has written prolifically on making a case for investors to be socially responsible as part of their legal duties, see Benjamin J Richardson, *Socially Responsible Investment Law: Regulating the Unseen Polluters* (New York: Oxford University Press 2008), in turn exerting pressure upon corporations to meet those expectations.

²⁷ United Nations, *Principles of Responsible Investment* <http://www.unpri.org/about-pri/the-six-principles/>.

²⁸ Joakim Sandberg, 'What are your Investments Doing Right Now?' in Wim Vanderkerckhove and others (eds), *Responsible Investment in Times of Turmoil* (Dordrecht: Springer 2011), 165ff; Carlos Joly, 'Reality and the Potential of Responsible Investment' and Riikka Sievänen, 'Responsible Investment by Pension Funds after the Financial Crisis' in Wim Vanderkerckhove and others (eds), *Responsible Investment in Times of Turmoil* (Dordrecht: Springer 2011), 193, 93ff respectively; showing that most pension funds never really developed novel or unique strategies for SRI.

FTSE4Good) could culminate in market messages to companies.²⁹ There is an increasing trend towards relying on investors, which are largely institutions regarded as representing the saving citizenry, to galvanise change in corporate behaviour.³⁰ Such influence however tends to be incremental and inherently subject to contesting objectives.³¹ The 'stewardship'³² of institutions is far from addressing public goods in a consistent and stable manner.³³

On the whole corporations have made some but slow progress in addressing the gap between corporate social performance and social expectations.³⁴ Where gaps persist between voluntary corporate social performance and social expectations, the introduction of regulatory governance may be appropriate. Regulatory leadership in governing corporate behaviour has been incremental but persistent, a phenomenon described as 'regulatory capitalism' (see below). Regulatory governance benefits from being able to frame socially expected standards of behaviour in public interest, capable of consistent application and enforceable by the means of a coercive order. Its potential drawback may however be its 'one size fits all' nature. The next Section discusses briefly milestones in contemporary corporate regulation and the significant surge in social appetite for corporate regulation post the global financial crisis 2007-9.

The Evolution of Corporate Regulation

²⁹ Luc Renneboog, Jenke ter Horst and Chendi Zhang, 'Socially Responsible Investments: Methodology, Risk Exposure and Performance' (June 2007) ECGI Finance Working Paper No 175/2007 http://papers.ssrn.com/sol3/papers.cfm?abstract_id=985267 ; Michael L Barnett and Robert M Salomon, 'Beyond Dichotomy: The Curvilinear Relationship between Social Responsibility and Financial Performance' (2006) 27 Strategic Management Journal 1101 Peer C Osthoff and Alexander Kempf, 'The Effect of Socially Responsible Investing on Portfolio Performance' (2005) 13 European Financial Management 908.

³⁰ The vision of fiduciary capitalism initially mooted by JP Hawley and AT Williams, *The Rise of Fiduciary Capitalism: How Institutional Investors Can Make Corporate America More Democratic* (University of Pennsylvania Press, 2000). But this vision has been questioned by commentators who view institutions and their fund managers as being subject to myopia and agency problems, see Ronald J Gilson and Jeffrey N Gordon, 'Agency Capitalism: Further Implications of Equity Intermediation' (2014) at <http://ssrn.com/abstract=2359690>; L Randall Wray, 'Money Manager Capitalism and the Global Financial Crisis' (2009) at <http://ssrn.com/abstract=1478508>.

³¹ Scepticism also expressed in Beate Sjafell, 'Regulating Companies as if the World Matters: Reflections from the Ongoing Sustainable Companies Project' (2012) 47 Wake Forest Law Review 113.

³² UK Stewardship Code 2016 that sets out engaged but constructive behaviour expected of institutions.

³³ The engagement of different types of institutional investors with their companies is fleshed out in Roger M Barker and Iris H-Y Chiu, *Investment Management and Corporate Governance in the Financial Economy* (Cheltenham: Edward Elgar, 2017), forthcoming.

³⁴ Empirical research found some voluntary programs to be largely rhetorical in nature, where corporations give the impression of outreach and engagement but in fact do little to change their social responsibility performance. See Cary Coglianese and Jennifer Nash, 'Performance Track's Postmortem: Lessons from the Rise and Fall of EPA's 'Flagship' Voluntary Program' (2014) 38 Harvard Environmental Law Review 1; David Vogel, 'The Private Regulation of Global Corporate Conduct: Achievements and Limitations' (2010) 49 Business and Society 68.

Regulating corporations is as old as corporate capitalism. Since the great privatisations and modernisation of Western economies from the 1980s,³⁵ corporations have played a leading role in economic activities as private actors and in markets. Nevertheless, the rise of the regulatory state is commensurate with the expansion of the corporate footprint, a phenomenon termed as 'regulatory capitalism'.³⁶ Regulatory capitalism refers to the existence of governance frameworks that shape economic functioning and protect certain political or social values, representing a landscape where economic functions and needs are facilitated, and where distributive or social goals are also pursued.³⁷ In other words, the public character of governance continues to exist extensively with the economic activities led by the private sector.

Corporate regulation is a powerful means to change corporate behaviour where such behaviour adversely affects the efficient working of markets or other social and public interest.³⁸ The development of corporate regulation in the UK can be traced to the litany of corporate scandals since the South Sea Bubble of the early eighteenth century.³⁹ Often increasing legalisation signals policy-makers' resolve to respond to social pressures that private corporations have failed to adequately address.⁴⁰ Corporate regulation reforms have taken the form of corporate duties such as in securities regulation as well as other external public interest regulation such as health and safety, product liability, occupier's liability and more recently compulsory occupational pensions provision.⁴¹ For example, corporate scandals in the UK in the 1990s involving financial reporting have led to reforms in both corporate reporting and governance in publicly listed companies.⁴² Scandals in the

³⁵ Claude V Chang, *Privatisation and Development: Theory, Policy and Evidence* (Aldershot: Ashgate, 2006) at chapters 1 and 2; Florencio López de Silanes, Andrei Schleifer and Robert W Vishny, 'Privatization in the United States' (1997) *RAND Journal of Economics* 447 at http://scholar.harvard.edu/files/shleifer/files/privatization_us.pdf; Dennis Swann, *The Retreat of the State: Deregulation and Privatisation in the UK and US* (Harvester Wheatsheaf, 1988); Richard Heffernan, 'UK Privatisation Revisited: Ideas and Policy Change, 1979–92' (2005) 76 *The Political Quarterly* 264.

³⁶ David Levi-Faur, 'The Global Diffusion of Regulatory Capitalism' (2005) 598 *The Annals of the American Academy of Political and Social Science* 12.

³⁷ John Braithwaite, *Regulatory Capitalism* (Cheltenham: Edward Elgar 2008), 4-29.

³⁸ See Michael Moran, 'The Rise of the Regulatory State' in David Coen et al (eds), *The Oxford Handbook of Business and Government* (Oxford: OUP 2010) at ch16.

³⁹ Mandatory requirements in early company law regarding formation of joint stock companies and transparency from the Joint Stock Companies Act 1844 to the Companies Act 1862.

⁴⁰ Such as workmen's compensation in the UK since 1897.

⁴¹ Not to mention the ambiguity about labour law in terms of being part of or external to 'corporate law'. The literature on this is too vast to cite, but see Lord Wedderburn of Charlton, 'Legal Development of Corporate Responsibility' in Klaus J Hopt and Gunther Teubner (eds), *Corporate Governance and Directors' Liabilities* (Berlin/NY: W de Gruyter, 1985) on an overview of the nature of company law and reform in corporate regulation in the UK.

⁴² The Cadbury Code of Corporate Governance introduced in 1992 in response to the failures of Polly Peck, Maxwell and BCCI.

UK involving mass deaths as a result of industrial or corporate accidents culminated in the enactment of the Corporate Homicide Act 2007.⁴³

There has however been marked resistance to reform company law to engage with wider or social responsibility, as company law remains a private, consensual paradigm.⁴⁴ This has resulted in limitations in advancing corporate legal responsibility such as liability for enterprise harms.⁴⁵ Moreover, the limitations of corporate regulation are unravelled in the context of multi-national corporations that have transnational footprint and may not be adequately controlled by any one state's regulatory controls.⁴⁶ Besides the transnational corporation may undermine states' resolve to adequately regulate them, as states engage in regulatory competition to attract their investment.⁴⁷ Transnational corporations have coalesced incredible influence as epistemic groups that influence knowledge production relating to issue areas and policy thinking,⁴⁸ as well as lobbying power.⁴⁹

Despite some achievements in corporate regulation that delineate expectations of corporate accountability and behaviour, it remains challenging to compel corporations to internalise responsibilities for social externalities or promote stakeholder inclusion.⁵⁰ However, non-traditional and reflexive forms of governance⁵¹ have been increasingly introduced for companies, especially

⁴³ CMV Clarkson, 'Kicking Corporate Bodies and Damning Their Souls' (1996) 59 *Modern Law Review* 557; David Ormerod and Richard Taylor, 'Legislative Comment: The Corporate Manslaughter and Corporate Homicide Act 2007' (2008) *Criminal Law Review* 589.

⁴⁴ Wedderburn (1985), above on the insularity of company law.

⁴⁵ Such as *Adams v Cape Industries plc* [1990] Ch 433, whose position is not significantly advanced by the narrow decision in *Chandler v Cape plc* [2012] EWCA Civ 525.

⁴⁶ Janet Dine, 'Transnationals out of Control' in *Governance of Corporate Groups* (Cambridge University Press 2000, 2006); Larry Cata Backer, 'The Autonomous Global Enterprise: On the Role of Organizational Law Beyond Asset Partitioning and Legal Personality' (2006) 41 *Tulsa Law Journal* at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=880730.

⁴⁷ Colin Crouch, 'The Global Firm: The Problem of the Giant Firm in Democratic Capitalism' in David Coen et al (eds), *The Oxford Handbook of Business and Government* (Oxford: OUP 2010) at ch6; but see Horst Eidenmüller, 'The Transnational Law Market, Regulatory Competition, and Transnational Corporations' (2011) 18 *Indiana Journal of Global Legal Studies* 707 who expounds on the powerful forces of regulatory competition but argues that regulatory competition allows corporations to escape from bad law as a result of poor policy choice in states, and should overall be supported.

⁴⁸ Eg Katherine E Smith, Gary Fooks, Anna B Gilmore and Jeff Collin, 'Corporate Coalitions and Policy Making in the European Union: How and Why British American Tobacco Promoted "Better Regulation"' (2015) 40 *Journal of Health Politics, Policy and Law* 325 on how the tobacco industry influenced policy-making frameworks in terms of economic-based assessments.

⁴⁹ Eg see David L Levy and Aseem Prakash, 'Bargains Old and New: Multinational Corporations in Global Governance' (2003) 5 *Business and Politics* 131-150.

⁵⁰ Resisted by the private nature of company law, see for eg Mark Pendras, 'Law and the Political Geography of US Corporate Regulation' (2011) 15 *Regulation, Space and Polity* 1, arguing that the efficiency perspective of the corporate organisation is often used as a shield against intrusive corporate law reform.

⁵¹ also Gunther Teubner, 'Substantive and Reflexive Elements in Modern Law' (1983) 17 *Law and Society Review* 239.

where traditional command-and-control techniques in regulating corporations are inappropriate.⁵² These to an extent mitigate the lack of achievement in company law reform.

The Growth of Reflexive Governance Techniques in Corporate Regulation

Reflexive techniques in regulation and governance have grown to secure the elusive goal of corporate behavioural change. Reflexive techniques may involve (a) a plurality of actors in designing governance thinking and techniques, and/or in securing compliance or enforcement at national or transnational levels; (b) a spectrum of norms, standards, arrangements or expectations along a soft-hard continuum, sometimes backed by law or regulatory enforcement and (c) a blurring of the distinction between public or private in terms of the source of and capacity for providing governance.

Ford terms such regulatory techniques as ‘flexible regulation’,⁵³ while Gilad uses the term ‘process-oriented’ regulation to describe this family of regulatory techniques.⁵⁴ For example, principles or outcomes-based regulation⁵⁵ can be introduced where certain known outcomes are prescribed in regulation while leaving a certain amount of discretion and responsibility to firms to take actions to ensure the attainment of those outcomes. However, outcomes-based regulation may be inappropriate where the certainty of outcomes cannot be defined, and process-based regulation may be more apt.

Process-based regulation focuses more on systems and internal procedures which approximate to soundness of control and governance, where outcomes may be undefined or heterogenous. For example, ‘management-based regulation’⁵⁶ emphasises organisational innovation and procedures to meet public regulatory goals. ‘Meta-regulation’⁵⁷ refers to a regulatory approach that empowers and enhances the capacity of corporations to self-regulate, but connects ‘the private justice of the internal management system’ to the ‘public justice of accountability’.⁵⁸ Process-based regulatory

⁵² See discussion in Iris H-Y Chiu and Anna Donovan, ‘A New Milestone in Corporate Regulation: Procedural Legalisation, Standards of Transnational Corporate Behaviour and Lessons from Financial Regulation and Anti-Bribery Regulation’ (2017) *Journal of Corporate Law Studies*, forthcoming.

⁵³ Cristie Ford, ‘Macro- and Micro-Level Effects on Responsive Financial Regulation’ (2011) 44 *University of British Columbia Law Review* 589.

⁵⁴ Sharon Gilad, ‘It Runs in the Family: Meta-regulation and its Siblings’ (2010) 4 *Regulation and Governance* 485.

⁵⁵ Mary Condon, ‘Canadian Securities Regulation and the Global Financial Crisis’ The Walter S Owen Lecture, University of British Columbia, 26 March 2009.

⁵⁶ Cary Coglianese and David Lazer, ‘Management-Based Regulation: Prescribing Private Management to Achieve Public Goals’ (2003) 37 *Law and Society Review* 691.

⁵⁷ Cary Coglianese and Evan Mendelson, ‘Meta-Regulation and Self-Regulation’ in R Baldwin, M Cave, and M Lodge (eds), *The Oxford Handbook of Regulation* (Oxford University Press, Oxford), pp. 146–168; Christine Parker, *The Open Corporation* (Cambridge: CUP 2002); ‘Meta-Regulation: Legal Accountability for Corporate Social Responsibility’ (2006) at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=942157; Colin Scott, ‘Regulating Everything: From Mega- To Meta-Regulation’ (2012) 60 *Administration* 61.

techniques are often collectively known as ‘new governance.’⁵⁹ New governance regulatory techniques are essentially reflexive and co-opt the regulated entities to develop effective compliance practices.

Increasingly we see corporate regulation framed as process-based regulation as corporations are mandated to change internal structures and governance, in a bid towards changing corporate behaviour and outcomes. This has been adopted in the UK’s Bribery Act 2010 to combat corrupt business practices, Criminal Finances Act 2017 to combat corporate complicity in money laundering and financial crime, as well as tax evasion, and the Modern Slavery Act 2015 to deal with abject labour and supply chain practices. These techniques circumvent the need to intrude upon the ‘private nature’ of company law, yet attempt to institute public interest expectations of internal governance and control.

However, reflexive techniques in regulation have suffered various criticisms. First, process-based regulatory techniques may result in excessive proceduralisation, disengaged from the ultimate purpose of changing corporate behaviour.⁶⁰ Firm implementation of procedures may be mechanistic and “box-ticking”⁶¹ in nature, fostering merely cosmetic forms of compliance.⁶²

Further, firm procedures, especially if presented as complex systems and technologies, provides an impression of endeavour, credibility and legitimacy and thus justify themselves, creating a form of legal endogeneity. Legal endogeneity occurs when the systems and procedures implemented by firms are taken as capable of defining what the needs of substantive justice or regulation are.⁶³ Legal endogeneity may obscure whether there is real engagement with the corporate social responsibility issues at hand or real changes in corporate behaviour.

Increasing Legalisation in Refining New Governance Techniques

Reflexive governance techniques are susceptible to compromising regulatory leadership altogether if they become excessively ‘delegated’ to the firm, tantamount to being self-regulatory in nature. Such critique⁶⁴ against reflexive governance techniques intensified in the aftermath of the global financial

⁵⁸ Christine Parker, *The Open Corporation* (Cambridge: Cambridge University Press 2000), 246.

⁵⁹ Cristie Ford, “New Governance, Compliance, and Principles-Based Securities Regulation” (2008) 45 *American Business Law Journal* 1.

⁶⁰ Omari Scott-Simmons, ‘The Corporate Immune System: Governance from the Inside Out’ (2013) *University of Illinois Law Review* 1131.

⁶¹ Michael Power, *Organised Uncertainty* (Oxford: Oxford University Press 2007) at 164.

⁶² Kimberly Krawiec, ‘Cosmetic Compliance and the Failure of Negotiated Governance’ (2003) 81 *Washington University Law Quarterly* 487.

⁶³ Russell J Funk and Daniel G Hirschman, “Endogenous Legal Change: How Organizations Re-Shaped Glass-Steagall” (University of Michigan Working Paper 2012).

⁶⁴ See Cristie Ford, ‘New Governance in the Teeth of Human Frailty: Lessons from Financial Regulation’ (2010) *Wisconsin Law Review* 441.

crisis 2007-9 which saw the loss of social confidence in modern capitalism⁶⁵ and the financial sector. An adjustment in the design of reflexive regulatory techniques has been taking place. The public-private mix in reflexive governance, which leaned heavily towards delegated self-regulatory efforts by the private sector has become characterised by greater intensity in public sector-backed governance.⁶⁶

There is expanding appetite⁶⁷ for subjecting corporate behaviour to greater intensity in regulatory governance. For example, there is a markedly sharper social appetite for the regulation of banks⁶⁸ in relation to their internal governance and external conduct. Combatting corporate tax evasion more generally is also a post-crisis initiative.⁶⁹

Hard law is enjoying a rejuvenation of credibility.⁷⁰ This is consistent with the cycles of regulation that follow the culmination of corporate failings and crises.⁷¹ Corporate regulation is able to espouse standards of behaviour and therefore chimes with social expectations, and to an extent, the needs for corporate compliance could change corporate behaviour.⁷² Corporate regulation represents a coalescence of social hope and political resolve, but its effectiveness in securing real and fundamental corporate behavioural change remains a challenging issue. State-backed authority is neither a panacea nor is substitutive for the range of governance dimensions that other actors bring. Hence, what we concomitantly observe greater legalisation in the form of adjustments to the new governance regulatory techniques instead of a resumption of command-and-control.

⁶⁵ Luiz Carlos Bresser-Pereira, 'The Global Financial Crisis and a new Capitalism' (May 2010, Levy Economics Institute); MK Brunnermeier and others, *The Fundamental Principles of Financial Regulation* (Geneva Reports on the World Economy, London: Centre for Economic Policy Research 2009) explicating the shortfall in regulating finance in the pre-crisis era.

⁶⁶ Cristie Ford, 'New Governance in the Teeth of Human Frailty: Lessons from Financial Regulation' (2010) *Wisconsin Law Review* 441.

⁶⁷ Engobo Emeseh, Rhuks Ako, Patrick Okonmah, Obokoh, Lawrence Ogechukwu, 'Corporations, CSR and Self Regulation: What Lessons from the Global Financial Crisis?' (2010) 11 *German Law Journal* 230; Larry Catá Backer, 'From Moral Obligation to International Law: Disclosure Systems, Markets and the Regulation of Multinational Corporations' (2008) 39 *Georgetown Journal of International Law* 591.

⁶⁸ There is a copious amount of literature on this, from policy papers to academic discussions. See Mads Andenas and Iris H-Y Chiu, *The Foundations and Future of Financial Regulation* (Oxford: Routledge, 2014) at chapters 1-3 and citations therein.

⁶⁹ See Iris H-Y Chiu, 'From Multilateral to Unilateral Lines of Attack: The Sustainability of Offshore Tax Havens and Financial Centres in the International Legal Order' (2016) 31 *Connecticut Journal of International Law* 177.

⁷⁰ Sybren C. de Hoo and Mieke Olaerts, 'Sustainable Development and the Need for Sustainable Oriented Corporate Law and Regulation' (2011) at <http://ssrn.com/abstract=1926065>; Jette Knudsen, 'Bringing the State Back in? US and UK Government Regulation of Corporate Social Responsibility (CSR) in International Business' (2014) at <http://ssrn.com/abstract=2541002>.

⁷¹ See Thomas Clarke, "Cycles of Crisis and Regulation" (2004) 12 *Corporate Governance* 153.

⁷² Christine Parker and Vibeke Lehmann Nielsen, 'Corporate Compliance Systems : Could They Make Any Difference?' (2009) 41 *Administration and Society* 3.

It is in this context we evaluate the recent mandatory disclosure reforms in the EU and UK with regard to social responsibility issues. Essentially mandatory disclosure is used as a conduit to prescribe the institutionalisation of internal processes in order to improve a firm's social responsibility consciousness and accountability. This technique in particular leverages upon the polycentricity of the governance landscape and provides opportunities for social governance to support regulatory obligations.

B. Disclosure-based Procedural Regulation in the EU and UK

Mandatory disclosure for corporations in the EU and UK has always been based on investors' needs. Early initiatives in the UK that incorporate aspects of social responsibility are based firmly on that tenet.⁷³ The UK has since 2006 required the directors' business review, a narrative report, to contain information on how environment and stakeholder issues relate to business performance.⁷⁴ The EU has to date extensively harmonised corporate reporting requirements including financial and narrative reporting.⁷⁵ The narrative reporting requirements relate to qualitatively explaining business performance and risks.⁷⁶ Narrative reporting in the EU and UK has, until the transformational reform introduced in the EU Non-financial Disclosure Directive 2014, been focused on shareholder-centric needs in relation to evaluating financial performance and viability.⁷⁷

In 2014 the EU introduced the Non-financial Disclosure Directive⁷⁸ inserting Article 19a into the 2013 Directive (referred to above) that deals with corporate reporting obligations. Article 19a requires large undertakings that are public-interest entities (exceeding on their balance sheet dates the

⁷³ For eg the superseded s417 of the UK Companies Act that deals with directors' business reviews- containing social responsibility matters framed as being useful for investors to understand the risks and performance of the company.

⁷⁴ The former 417, Companies Act 2006 since superseded by s414A, the Strategic Report, discussed in Iris H-Y Chiu, 'Reviving Shareholder Stewardship: Critically Examining the Impact of Corporate Transparency Reforms in the UK' (2014) 38 Delaware Journal of Corporate Law 983 and now supplemented by s414CA which transposes new narrative reporting requirements introduced in the EU Non-financial Disclosure Directive 2014, to be discussed shortly in the main text.

⁷⁵ Directive 2013/34/EU of the European Parliament and of the Council of 26 June 2013 on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings, amending Directive 2006/43/EC of the European Parliament and of the Council and repealing Council Directives 78/660/EEC and 83/349/EEC.

⁷⁶ Also future development, research and development, adherence or otherwise to any corporate governance code and the state of the company's risk management and internal control, see Arts 19-20, Directive 2013/34/EU above.

⁷⁷ Iris H-Y Chiu, 'The Paradigms for Mandatory Non-Financial Disclosure: A Conceptual Analysis- Parts 1 and 2' (2006) *Company Lawyer* 259; 291. On the shareholder-centric focus of the s417 directors' report, see Ian Havercroft and Arad Reisberg, "Directors' Duties Under the UK Companies Act 2006 and the Impact of the Company's Operations on the Environment" (2010) at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1274567; Andrew Keay, "Section 172(1) of the Companies Act 2006: an Interpretation and Assessment" (2007) 28 *Company Lawyer* 106.

⁷⁸ Directive 2014/95/EU of the European Parliament and of the Council of 22 October 2014 amending Directive 2013/34/EU as regards disclosure of non-financial and diversity information by certain large undertakings and groups.

criterion of the average number of 500 employees during the financial year) to include in the management report a **non-financial statement** containing **information to the extent necessary for an understanding of the undertaking's development, performance, position and impact of its activity, relating to, as a minimum, environmental, social and employee matters, respect for human rights, anti-corruption and bribery matters**. This is transposed in the UK which now requires the directors' Strategic Report, i.e. the narrative report produced by the Board, to include a non-financial information statement that contains the above-highlighted information.⁷⁹

The EU's and UK's new mandatory disclosure requirement arguably relates to reviewing the corporation's social responsibility and stakeholder relations as standalone matters, and not only as matters relevant to the business case. We take a different position from that argued by Choudhury⁸⁰ in relation to the primary relevance and utility of social disclosure to investors. Investors may not be uninterested in these matters,⁸¹ but in these reforms, the mandatory disclosure is not constrained or shaped by a shareholder-centric focus. These reforms pertain to connecting the needs of social justice to corporate regulation.⁸²

The Directive states clearly in its preamble⁸³ that the non-financial reporting relates to needs in improving the accountability of corporate social responsibility relevant to stakeholders such as consumers besides investors. This distinguishes the mandatory non-financial information statement from other shareholder-centric financial and non-financial reporting referred to above. We arguably see the new mandatory reporting requirements as introducing a new kind of corporate transparency framed towards social and public accountability. A caveat that can be introduced here is that upon the UK's departure from the EU, the preamble may no longer apply in the UK's interpretation of the nature of the non-financial information statement.

However, it can be argued that as the non-financial information statement is required 'to be included' in the 'management report' (i.e. the UK's directors' Strategic Report), the statement takes after the character of the Report, which is non-financial reporting supporting the company's **financial** transparency. Further, as the non-financial disclosure in the Strategic report is guided by a standard of materiality,⁸⁴ which refers to whether the disclosure matters for the investment

⁷⁹ Section 414CA, inserted into the Companies Act 2006 via the via the Companies, Partnerships and Groups (Accounts and Non-Financial Reporting) Regulations 2016 (S.I. 2016/1245).

⁸⁰ Barnali Choudhury, 'Social Disclosure' (2016) 13 Berkeley Business Law Journal 183.

⁸¹See Ian B Lee, 'Corporate Law, Profit Maximization and the "Responsible" Shareholder' (2004) 10 Stanford Journal of Law, Business and Finance 31; but see Virginia Harper Ho, "'Enlightened Shareholder Value": Corporate Governance Beyond the Shareholder-Stakeholder Divide' (2010) 36 Journal of Corporation Law 59 and sceptical comments on this concept by Paul Davies, 'Enlightened Shareholder Value and the New Responsibilities of Directors' (2005) at http://law.unimelb.edu.au/__data/assets/pdf_file/0014/1710014/94-Enlightened_Shareholder_Value_and_the_New_Responsibilities_of_Directors1.pdf.

⁸² See Preamble 3, EU Non-financial Disclosure Directive 2014.

⁸³ Preamble 3.

⁸⁴ Financial Reporting Council, *Guidance on the Strategic Report* (June 2014) at Section 5.

decisions of a reasonable investor,⁸⁵ the non-financial information statement could be governed by the same shareholder-centric standard.

We however support the contrary position that the non-financial information statement is distinct, and argue that the materiality standard recommended by the Financial Reporting Council may require revision. It is also to be noted that the Global Reporting Initiative has introduced a concept of materiality for environment and social impact in order to guide management in making social responsibility disclosures in accordance with the GRI's Reporting Standards. Hence it is not necessary that 'materiality' should be a shareholder-centric benchmark.⁸⁶

Support for the distinctness of the non-financial statement can be found in the prescribed matters to be disclosed. These matters relate ultimately to evaluating a company's social responsibility performance, and can be distinguished from shareholder-focused financial or non-financial reporting.

The Directive provides that the non-financial information statement must disclose:

- (a) a brief description of the group's business model;
- (b) a description of the policies pursued by the group in relation to [the social responsibility] matters [mentioned above], including due diligence processes implemented;
- (c) the outcome of those policies;
- (d) the principal risks related to those matters linked to the group's operations including, where relevant and proportionate, its business relationships, products or services which are likely to cause adverse impacts in those areas, and how the group manages those risks;
- (e) non-financial key performance indicators relevant to the particular business.

The UK transposition differs slightly by specifying that each of the matters to be disclosed is 'a description' in nature. This may raise certain implications in our interpretational study to be shortly discussed.

First, the non-financial information statement must contain a description of the company or in the case of a consolidated statement for groups, the group's business model. The description is qualified by the relevance of such information to the **development, performance, position and impact of its activity, relating to, as a minimum, environmental, social and employee matters, respect for human rights, anti-corruption and bribery matters**. This requirement compels companies to identify the aspects of its business activity that relate to the social responsibility and stakeholder areas above, not the converse. Companies therefore need to have regard for their social responsibility performance as such and not merely relegate the relevance of social responsibility performance to business and financial performance.

⁸⁵ See also Daniel Szabó, 'Disclosure of Material CSR Information in the Periodic Reports – Comparison of the Mandatory CSR Disclosure Systems for Listed Companies in the EU and the US' (2011) at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=1927232.

⁸⁶ GRI Reporting Standards, *Management Approach* (2016) at <https://www.globalreporting.org/standards/gri-standards-download-center/?g=af5e723a-0759-40e6-a1a8-01fe0c6ab3d1>.

Further, the company must disclose a description of the policies pursued in relation to the social responsibility and stakeholder matters and any due diligence processes implemented. It is curious to note that the requirement of disclosure pertains to a *description* of the company's policies, meaning that company policies are not required to be laid bare as such to the public. The privacy of company policies is preserved and only a description need be provided. It may be argued that such a formulation for disclosure could encourage rather broadly-framed narratives in general terms. However, further disclosure requirements in relation to due diligence processes and the outcomes of policies may mitigate against the risk of broadly framed or meaningless disclosure.

Procedural Regulation- Due Diligence Processes

In requiring disclosure of the company's due diligence processes, the transparency requirement in the Directive should not be taken at face value. This transparency requirement indeed introduces an indirect procedural requirement for the company to institute due diligence processes, and should not be regarded as regulatory technique focused on information. In order to make disclosure of such procedures, companies are compelled to establish them. Mandatory disclosure indirectly introduces a form of procedural regulation.

It is possible that companies can choose to make disclosure of their due diligence procedures in broad terms. In particular, the disclosure obligation in the UK refers to a ***description*** of the procedures. General non-financial reporting (under Arts 19 and 20 of the EU Directive on Corporate Transparency of 2013 or the UK's Strategic Report in s414A, Companies Act 2006) already requires reporting on companies' risk management and internal control. Thus, companies can subsume reporting on due diligence procedures for social responsibility into risk management disclosure generally.⁸⁷ This would be a relatively incremental way of responding to the new disclosure obligation.

We do not think such minimal treatment would pass muster. Stakeholders, as well as shareholders who are not apathetic to such disclosure may find such minimal treatment to be non-compliant, as one can interpret the disclosure obligation as relating to due diligence procedures in relation to each relevant social responsibility area. We see this form of procedural regulation as intending to achieve the effect of compelling companies to demonstrate change and reform to their internal procedural and governance frameworks, as a proxy for demonstrating behavioural change. Further, the itemisation in the disclosure obligation in relation to: company due diligence procedures, non-financial performance indicators for the social responsibility matters and evaluation of outcomes- all require a certain engagement with substantive reporting whose quality will be scrutinised.

As procedural change and response is needed, companies may find it appealing to look to due diligence frameworks that enjoy social endorsement in order to enhance the substantive quality of their implementation and disclosure. Civil society initiatives offer ready-made and credible templates and frameworks at the *input* stage for companies.

⁸⁷ Due diligence is often developed as part of a company's risk management and internal control as a matter of its 'operational' location, see Chandra S Mishra, *Proof of Concept, Due Diligence, Risk and Reward* (Basingstoke: Palgrave Macmillan 2015).

There are various third-party frameworks already in existence that provide guidance on how due diligence procedures can be constructed and disclosed. In fact the existence of these frameworks provide a benchmark against which to measure corporate disclosure, and corporations may be incentivised to adopt them as being 'bonded' to them could be socially appealing. The inability of corporate regulation to be excessively prescriptive about due diligence procedures, given the need for such procedures to be context-specific, provides an opportunity for civil society groups to offer bottom-up initiatives to engage with corporations, giving rise to a form of pluralistic procedural regulation. Regulation, civil society and the regulated corporation can engage in a dynamic manner to achieve changes in corporate behaviour.⁸⁸

In terms of environmental protection, companies may look to the ISO14001 process-based standard for environmental management, which has attained a credible stature. Prakash in his detailed examination of ISO14001 explains that the standard comprises of various management processes that have to be established in a company, including an environment policy and its governance, an environment plan including stakeholder engagement, environmental objectives such as setting targets and dedicating resources, environmental impact assessments and the organisational management of environmental issues including integration into strategic management.⁸⁹ Companies are independently audited in order to be certified for the standard, and empirical research shows that the adoption of the ISO14001 has improved the environmental consciousness and protection performance on the part of companies.⁹⁰

Human rights due diligence has also been developed following the introduction of the UN Guiding Principles that seek to operationalise human rights protection and redress of human rights breaches by states and corporations.⁹¹ For example, commentators have identified contexts for due diligence, such as in early stages of contractual negotiations and procurement, and in on-going monitoring and review.⁹² In particular, leading due diligence standards have been produced by SHIFT and Mazars,⁹³ in the form of systematic diagnostic questions designed to lead companies into thinking about and instituting relevant processes.⁹⁴ Companies are guided to consider their management, governance

⁸⁸ David Wirth, 'The International Organization for Standardization: Private Voluntary Standards as Swords and Shields' (2009) 36 Boston College Environmental Affairs Law Review 79.

⁸⁹ Aseem Prakash, *The Voluntary Environmentalists* (Cambridge: CUP 2009).

⁹⁰ Above.

⁹¹ John Ruggie, "Guiding Principles on Business and Human Rights: Implementing the United Nations 'Protect, Respect and Remedy' Framework" (2011) at http://www.ohchr.org/Documents/Publications/GuidingPrinciplesBusinessHR_EN.pdf.

⁹² Mark B Taylor, Luke Zandvliet and Mitra Forouhar, 'Due Diligence for Human Rights: A Risk-Based Approach' (2009) at https://www.hks.harvard.edu/m-rcbg/CSRI/publications/workingpaper_53_taylor_etal.pdf.

⁹³ Larry Catá Backer, 'The Guiding Principles of Business and Human Rights at a Crossroads: The State, the Enterprise, and the Spectre of a Treaty to Bind Them All' (2014) at <http://ssrn.com/abstract=2462844>.

⁹⁴ The SHIFT framework for human rights due diligence in high risk contexts guide companies through identifying the context of risks such as in conflict areas or business relationships with partners with certain track records, business activities of a sensitive nature such as over water resources or in the presence of vulnerable groups such as aboriginal communities. Companies are then guided to identify the types of risks

and capacity to manage such risks, including information collation, senior management governance, embedding in enterprise risk management systems, the development of indicators to measure performance, and stakeholder engagement, including allowing stakeholders to push information to companies.⁹⁵ Harrison also proposes that human rights due diligence can be further made more robust in companies if they seek third party independent verification, so standards in relation to such verification or assurance would be a next step in development.⁹⁶

In terms of labour standards, the unifying core of labour rights and standards under the various International Labor Organization conventions have helped civil society groups to establish standards that help companies forge appropriate management processes and codes of conduct. Third party organisations are able to provide certification programs in order to verify companies' labour management practices including in supply chains.⁹⁷ Large retailers such as Gap, Nike and Reebok have established management processes according to the ILO standards, while organisations such as Social Accountability, The Fair Labor Association and the Dutch Clean Clothes Campaign provide certification programs for companies on a voluntary basis. For example the Social Accountability organisation's SA8000 certification processes comprise of reviews of documentation, working practices, employee interview responses, and operational records and on site visits before awarding the certification.⁹⁸

Anti-bribery and corruption is now part of corporate compliance in the UK,⁹⁹ and the Ministry of Justice issued 6 guiding principles¹⁰⁰ on the implementation of what may be regarded as 'adequate procedures' in preventing bribery. However, companies may find useful the Checklist developed by Transparency International that systematically directs companies to establish policies and management processes that would meet the broadly worded procedural requirements in the

that arise, including single, cumulative and combination of factors, and meta-factors such as conflict, presence of vulnerable groups, repressive regimes etc.

⁹⁵ SHIFT, *Human Rights Due Diligence in High Risk Circumstances: Practical Strategies for Businesses* (2015) at http://www.shiftproject.org/media/resources/docs/Shift_HRDDinhighriskcircumstances_Mar2015.pdf.

⁹⁶ James Harrison, 'An Evaluation of the Institutionalisation of Corporate Human Rights Due Diligence' (2012) at <http://ssrn.com/abstract=2117924>.

⁹⁷ Discussed in Dara O'Rourke, 'Outsourcing Regulation: Analyzing Nongovernmental Systems of Labor Standards and Monitoring' (2003) 31 *Policy Studies Journal* 1.

⁹⁸ Ongoing review is also carried out. The certification process is in relation to standards and management processes in key areas such as child labour, forced or compulsory labour, health and safety, freedom of association and right to collective bargaining, discrimination, disciplinary practices, working hours, remuneration and management system, see <http://www.sa-intl.org/index.cfm?fuseaction=page.viewpage&pageid=1689>.

⁹⁹ The Bribery Act 2010 criminalises various bribery acts but corporations may be able to defend themselves if they have established 'adequate procedures' to prevent bribery. See Anna P. Donovan, 'Systems and Controls in Anti-Bribery and Corruption', in Iris Hse-Yu Chiu and Michael McKee (eds), *The Law on Corporate Governance in Banks* (Edward Elgar, 2015), 236.

¹⁰⁰ The Ministry of Justice, *Bribery Act 2010: Guidance About Procedures which Relevant Commercial Organisations can put into Place to Prevent Persons Associated with them from Bribing* (section 9 of the Bribery Act 2010) (March 2011).

Bribery Act and MOJ Guidance. The Checklist deals with governance, policy setting and implementation, operational processes, training, external communications such as complaints and advice, internal control, information collation and reporting, membership in collective organisations and specific risk areas such as sponsorships, charitable and political donations, business relationships, contractors and suppliers, investments, joint ventures and consortia.¹⁰¹ Further, international organisations such as the UN Office for Drugs and Crime, World Bank and the OECD¹⁰² have also collectively produced a handbook to provide procedural insight and case study examples of good and poor practices.

Finally in general social responsibility, companies can look to the ISO26000 standard which is a guidance and not a certification standard. ISO26000 introduces a harmonised conception of social responsibility issues, largely drawn from global social responsibility standards such as the UN Global Compact, ILO conventions etc, and brings together an integrated approach towards governance, information collection and awareness, training, communications and stakeholder engagement.¹⁰³ The integrated approach has been criticised to pander excessively to the business case,¹⁰⁴ and it remains to be seen if the practices of social responsibility could so easily converge or be 'integrated', given that the due diligence needs in different issue areas may be rather different.

Mandatory disclosure with regard to due diligence procedures and implementation by companies introduces an indirect form of procedural regulation that opens up to public scrutiny and accountability. This accountability framework ushers in an opportunity for civil society and bottom-up initiatives to engage with companies, providing practical advice or guidance in implementing due diligence procedures. This form of engagement has the potential to promote a reflexive form of new governance where procedural regulation interacts with civil society governance in order to change corporate behaviour.

Procedural Regulation- Non-financial Key Performance Indicators and Outcomes

Art 19a of the EU Directive 2014 requires mandatory disclosure of companies' 'non-financial key performance indicators' and 'outcomes' of their social responsibility policies. Section 414CA of the UK Companies Act refers to a 'description' of such outcomes. It can be argued that section 414CA may only require a narrative overview of what the company's policies have achieved. We think the difference in language may be of some importance, however, there is a limit to how minimalist an interpretation can be made of section 414CA. This is because the section, like under the EU Directive, is aimed at focusing companies on ***measuring and evaluating social performance***. This requires a change in orientation and practices.

¹⁰¹ Transparency International, *Guidance on Good Practice Procedures for Corporate Anti-bribery Programmes* (2012) at <http://www.transparency.org.uk/publications/adequate-procedures-checklist-pdf/>.

¹⁰² OECD, *Anti-corruption Ethics and Compliance Handbook for Businesses* (2013) at <https://www.unodc.org/documents/corruption/Publications/2013/Anti-CorruptionEthicsComplianceHandbook.pdf>.

¹⁰³ See https://www.iso.org/files/live/sites/isoorg/files/archive/pdf/en/discovering_iso_26000.pdf.

¹⁰⁴ Andrew Johnston, 'ISO 26000: Guiding Companies to Sustainability Through Social Responsibility?' (2012) 9 European Company Law 110.

In terms of non-financial key performance indicators, companies may, if left to themselves, develop these as being complementary to financial performance indicators. As the non-financial information statement must include 'non-financial key performance indicators **relevant to the business**', it can be argued that the non-financial reporting of social responsibility matters ultimately relate to a wider understanding of business performance after all.¹⁰⁵ Nevertheless, it could also be counter-argued that '**relevant to the business**' refers to the social responsibility or stakeholder issues relevant to the company, i.e. arising out of the company's operations. Hence companies should interpret this requirement as relating to the **social performance of the business** and not the **social performance of the business as mediated through the business case**.

Civil society initiatives have taken steps towards developing more concrete indicators focused on social responsibility performance, therefore challenging the focus of businesses in terms of what they measure. Boesso¹⁰⁶ argues, in a comparative study of CSR reporting by US and Italian companies that predate the Non-financial Disclosure Directive 2014, that social responsibility matters identified in internationally recognised reporting templates such as the Global Reporting Initiative's standards often form the basis for developing non-financial key performance indicators. Companies develop measures for the matters specified by the GRI's Sustainability Reporting Standards.¹⁰⁷ The Standards identify clearly what is to be measured and reported under 'Economic', 'Environment' and 'Social' categories. For example, under 'Economic', anti-corruption achievements are to be reported, amongst other matters, such achievements are measured in relation to a list of items including extensiveness of training and intensity of internal risk management. Under 'Environment', firms are required to measure and report on items such as biodiversity and conservation of water resources. Further breakdown of what is to be measured in biodiversity and water conservation includes extent of water recycling, impact on biodiversity such as species reduction or habitat conversion etc. The high level of specificity and prescription in the GRI Reporting Standards provide a good proxy for the development non-financial key performance indicators in the relevant areas of economic, environment or social responsibility.

It is queried if disclosure of 'outcomes' would relate to formal impact assessments¹⁰⁸ that companies should carry out in all social responsibility matters referred to in the Directive. Impact assessments would compel companies to substantively and procedurally engage with their social impact and

¹⁰⁵ Such as a triple bottom line approach see John Elkington, Enter the Triple Bottom Line, in Adrian Henriques and Julie Richardson (eds), *The Triple Bottom Line, Does It All Add Up?: Assessing the Sustainability of Business and the CSR* 1, 1-16 (Earthscan 2004).

¹⁰⁶ Giacomo Boesso, 'Stakeholder Reporting and Voluntary Performance Indicators in Italian and U.S. Listed Companies' (2007) at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=968677.

¹⁰⁷ <https://www.globalreporting.org/information/g4/Pages/default.aspx>. The GRI Standards have long been regarded as internationally harmonising in nature, see KPMG International, *KPMG International Survey of Corporate Responsibility Reporting 2008* (2008), available at http://www.kpmg.com/US/en/IssuesAndInsights/ArticlesPublications/PressReleases/Documents/Corporate_Sustainability_Report_US_Final.pdf; Halina Szejnwald Brown, Martin De Jong, and Teodorina Lessidrenska. 'The rise of the Global Reporting Initiative: A Case of Institutional Entrepreneurship' (2009) 18 *Environmental Politics* 182-200.

¹⁰⁸ Gilliam MacNaughton, 'Human Rights Impact Assessment: A Method for Healthy Policymaking' (2015) 17 *Health and Human Rights* 63.

strategic decisions, and in our view would be optimal practice. These may however create rather costly burdens for companies. Further, as Harrison points out,¹⁰⁹ impact assessments may only be credible if carried out with the involvement of independent third parties, so cost in relation to obtaining verification or assurance may also be significant. We are of the view that disclosure of outcomes (which could be regarded as being more comprehensive in the Directive's wording than the UK's version of 'description' of outcomes) does not necessarily entail the production of impact assessments. However, as the non-financial disclosure statement can be subject to securities litigation by investors, the support of impact assessments may mitigate the risk of mis-disclosure by corporations. This would be relevant if stakeholders, like in the case of Nike discussed above, also have capacity to act in the space for shareholder enforcement.

Although the mandatory disclosure of due diligence procedures, non-financial key performance indicators and 'outcomes' remains susceptible to self-assessed and broad-based reporting, which is not helped by the UK's adoption of the term 'description' to all the elements of disclosure required, the availability of civil society templates and benchmarks provide to an extent, yardsticks for evaluating the quality of substantive compliance. These may also affect investor and regulators' perception of what adequacy means for disclosure and could influence enforcement actions that relate to insufficient or mis-disclosure. The indirect form of procedural regulation brought in by the mandatory disclosure requirement encourages corporations to recognise the expectations of public accountability, and may entice them to adopt and bond themselves to socially developed standards and procedures. Such forging of a pluralistic governance system is promising for bringing about changes to corporate behaviour, as regulation provides the law-backed framework for compliance while bottom-up initiatives offer practical application in increasingly established and definite ways. Next we turn to corporate transparency in the UK in relation to modern slavery. This regime applies a similar mandatory disclosure approach but engages to a lesser extent with indirect procedural regulation. We argue that the relatively poorer engagement with indirect procedural regulation is a missed step in the UK in relation to the potential of achieving richer and more effective forms of governance as highlighted above.

C. The UK's Mandatory Disclosure Provision in the Modern Slavery Act 2015

The UK enacted the Modern Slavery Act 2015 initially in response to combatting human trafficking crimes, but in the course of the debates over the draft Bill, campaigners¹¹⁰ sought to support greater corporate responsibility for supply chains and forced labour used therein. Hence, the Act now provides for certain corporations¹¹¹ to make mandatory disclosure yearly of a 'slavery and human trafficking statement' (the Statement) in order to provide transparency on the steps that a corporation has taken to ensure that its business and its supply chain are free from slavery and human trafficking.¹¹² Employment practices in the UK continue to be an issue of concern as in 2016,

¹⁰⁹ Above.

¹¹⁰ Eg see S. Lipscombe and O. Gay, *Modern Slavery Bill 2014-15, Bill 8 of 2014-15*, House of Commons Library Research Paper 14/37 (2 July 2014) 20

¹¹¹ Having a turnover over £36 million net of taxes, as prescribed by section 2, The Modern Slavery Act 2015 (Transparency in Supply Chains) Regulations 2015.

¹¹² Section 54, Modern Slavery Act 2015.

abusive and illegal employment practices at large UK sports retailer Sports Direct came to light and became the subject of a Parliament Inquiry.¹¹³

The Statement is less prescriptive in nature than the non-financial information statement discussed above. It refers to a list of matters similar to the non-financial information statement, but they are neither exhaustive nor mandatory. The list of matters includes:

- (a) the organisation's structure, its business and its supply chains;
- (b) its policies in relation to slavery and human trafficking;
- (c) its due diligence processes in relation to slavery and human trafficking in its business and supply chains;
- (d) the parts of its business and supply chains where there is a risk of slavery and human trafficking taking place, and the steps it has taken to assess and manage that risk;
- (e) its effectiveness in ensuring that slavery and human trafficking is not taking place in its business or supply chains, measured against such performance indicators as it considers appropriate; and
- (f) the training about slavery and human trafficking available to its staff.

Section 54 provides that companies *may* include the matters listed for disclosure and this is clarified by the Ministry's Practical Guidance as not being compulsory.¹¹⁴ The Practical Guidance emphasises that the Statement should encapsulate the steps taken by the company to prevent slavery and human trafficking in its business and supply chain. The Statement should also be in plain English, succinct and hence readily accessible.

By being less prescriptive about the matters to be disclosed, the mandatory disclosure obligation in section 54 of the Modern Slavery Act does not arguably give rise to the same intensity of procedural regulation as discussed above. In fact section 54 is more akin to meta-regulation as firms are able to design their systems and processes in order to meet the broad requirement of 'taking steps to prevent modern slavery and human trafficking'. Such reflexivity allows firms to apply the requirement flexibly within its business context, but as Wen argues, such a requirement may not prevent minimal or cosmetic demonstrations of processes and steps, especially as there is no obligation to bring in independent third party verification.¹¹⁵ Nevertheless, the Secretary of State has

¹¹³ House of Commons Business Innovation and Skills Committee, *Employment Practices at Sports Direct* (July 2016) at https://www.publications.parliament.uk/pa/cm201617/cmselect/cmbis/219/219.pdf?utm_source=219&utm_medium=module&utm_campaign=modulereports highlighting breaches of minimum wage regulation, employment law and abusive practices.

¹¹⁴ Home Office, *Transparency in Supply Chains etc: A practical guide* (2015) at https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/471996/Transparency_in_Supply_Chains_etc__A_practical_guide__final_.pdf.

¹¹⁵ Shuangge Wen, 'The Cogs and Wheels of Reflexive Law ± Business Disclosure under the Modern Slavery Act' (2016) 43 *Journal of Law and Society* 327.

the power to bring civil proceedings against any corporation to enforce the duties in section 54, which presumably includes the non-production of the Statement, or its inadequate production. There is some potential for the enforcement action to bring in a form of procedural governance, although its potency depends on how frequently it is brought and how it is framed. We are sceptical as to the potency of regulatory enforcement as the relevant regulator is the Home Office, which is tasked with more pressing social and crime enforcement responsibilities. It is possible that such enforcement could be carried out as part of a criminal enforcement action against a company for engaging in modern slavery, but we do not see the Home Office as an ongoing supervisor of companies' procedural systems and governance, or perhaps as watchman for corporate behavioural change. Hence, we are of the view that it is important to enrol stakeholder scrutiny for companies' internal governance and procedures, as well as their disclosure.

We carried out a brief survey of the first batch of Modern Slavery Statements and argue that although companies aim to comply at a high standard, there is a lack of engagement with social expectations in that regard. This is possibly due to the weaker nature of procedural governance provided in the Act.

The Table in Appendix 1 illustrates that the Statements largely converge on the list of matters required in the Act although that is not mandatory. A very cursory survey of sample firms in different sectors shows that they tend to treat the non-exhaustive list as a minimum template for disclosure. This practice secures some extent of comparability in the Statements produced. We find that companies rely solely on internally developed procedures to demonstrate due diligence and internally-generated performance indicators to assess outcomes. They do not seem to engage with stakeholder developed initiatives to reform procedural governance and do not demonstrate engagement with wider society expectations in this regard. We are of the view that the relatively weaker level of indirect procedural governance in the Act allows companies to be relatively insular, and does not go far enough to encourage companies to radically reform their internal procedures and governance. Although it may be argued that internal codes and procedures need not be inferior, they are still fundamentally self-generated and assessed, and not necessarily connected with notions of substantive quality consonant with social expectations.

For our purposes this paper compares on a qualitative basis six Statements produced by UK companies, namely Marks & Spencer Plc¹¹⁶ in the apparel retail sector, McMullen & Sons Ltd¹¹⁷ in the restaurant and pub management sector, the Go-Ahead Group Plc¹¹⁸ in the public transportation sector operating Southeastern rail services and regional bus services, Sirka UK Limited¹¹⁹ in the building and construction sector, the Economist Group¹²⁰ in the journalism sector and Associated

¹¹⁶ <https://corporate.marksandspencer.com/documents/plan-a-our-approach/mns-modern-slavery-statement-june2016.pdf>.

¹¹⁷ <http://www.mcmullens.co.uk/files/Slavery-Statement.pdf>.

¹¹⁸ <https://www.southeasternrailway.co.uk/-/media/goahead/southeastern/documents/policies/modern-slavery-statement.pdf>.

¹¹⁹ <http://gbr.sika.com/en/group/about-us/modern-slavery-statement.html>.

¹²⁰ http://www.economistgroup.com/pdfs/Modern_Slavery_statement.pdf.

British Foods Plc¹²¹ in the food manufacturing, processing and distribution sector. This is a cursory survey only and the sectors have been selected for their potential to employ low wage workers in the UK and/or supply chains abroad. The companies are different in size, scale and economic footprint, showcasing at least an extent of variety in the small sample surveyed.

The encouraging sign from this brief survey is that companies are cautious about even rather reflexive forms of regulation. They aim to show a form of compliance with procedural regulation, reflecting an awareness of the current climate where we see increasing juridification of corporate social responsibility issues. Companies perhaps recognise that such reflexive regulation can be a temporary state of affairs and can be scaled up towards more hardened forms of procedural regulation¹²² if they do not demonstrate change. However we also note that companies do not offer more disclosure than required under the non-exhaustive list of matters, and are especially short on specific risks where slavery or human trafficking may occur in the business or supply chain. This may be due to a fear of putting business-sensitive information into the public domain.

We discern that all subjects of the survey take steps to prevent slavery and human trafficking according to their own internal codes and guidelines and do not rely on externally established codes or guidelines by civil society or international organisations. This insular approach is susceptible to cosmetic or minimal change in internal governance. In this regard we question whether a stronger form of procedural governance such as discussed earlier is needed to stimulate change in companies. Nevertheless, there may be cross-fertilisation for the quality of Modern Slavery Statements if listed companies already adopt a socially-focused business and human rights due diligence for example. If a listed company complying with the Directive already institutes socially focused due diligence and social performance evaluation, there would be organisational efficiency reasons for streamlining their treatment the Modern Slavery statement. We see an opportunity for a larger-scale empirical survey, in a few years when data is available, comparing section 414CA reporting and modern slavery reporting. This would be important for determining the impact of strong forms of procedural regulation on corporate behaviour.

D. Critical Reflections and Conclusion

The increasing juridification of corporate social responsibility issues shows that what is regarded as 'voluntary' and 'good' behaviour may become socially expected and legally enforceable behaviour. However, change to corporate behaviour is not easily achieved, borne out by the evolution of both policy and technique in corporate regulation over the decades. Reflexive forms of regulation and civil society-led governance may on their own be insufficiently influential, but a form of complementarity brought about by the reforms discussed can unleash potential to change corporate behaviour.

We argue that the mandatory disclosure introduced in the non-financial information statement for EU and UK corporations¹²³ brings in a form of procedural regulation subject to multi-faceted spheres

¹²¹ https://www.abmauri.com/modern_slavery_act.pdf.

¹²² Discussed in Iris H-Y Chiu and Anna Donovan, 'A New Milestone in Corporate Regulation: Procedural Legalisation, Standards of Transnational Corporate Behaviour and Lessons from Financial Regulation and Anti-Bribery Regulation' (2017) *Journal of Corporate Law Studies*, forthcoming.

¹²³ And other businesses with a public interest element as defined under the Directive.

of accountability. In designing a form of procedural regulation under a mandatory disclosure framework, policy makers and civil society organisations continue to refine modern frameworks of governance in terms of aspects of softness and hardness along a spectrum that encourage effective change in behaviour. This approach departs from a market-based liberal framework that relies on investors to hold companies to account. Rather it seeks to empower stakeholders and civil society to engage with companies at an input level, influencing companies to adopt more socially-infused frameworks for due diligence and evaluating social performance.

Such a governance design relies on polycentric dialogue and influence, and less on clearly defined enforcement processes. Regulators provide fundamental support in standard-setting and ensuring comparability. This may however be criticised as stakeholders are not formally empowered under company law to hold companies to account and disclosure regulation can be regarded as ultimately pandering to the capital markets.¹²⁴ We see promise however in this form of *input-based* governance as facilitating learning-based behaviour. This form of reflexive governance marries the coercive power of mandatory transparency with civil society input and scrutiny into firms. However the UK's mandatory disclosure requirement for modern slavery and human trafficking falls short of introducing a form of procedural regulation and it will be crucial to discern any difference in quality of reporting and internal governance that entails.

We may argue that indirect procedural regulation subsumed under mandatory disclosure is a half-hearted technique and does not go far enough to legalise corporate responsibilities. Why not institute directors' duties to ensure procedural compliance,¹²⁵ or as Taylor suggests, implement the proposal mooted by the French to impose a duty of care for business responsibility on parent corporations so that they may be liable for the negative externalities their activities generate?¹²⁶ We acknowledge that this governance technique skirts rather than reforms the heart of corporate law, and is by no means the silver bullet or final word on effecting corporate social responsibility.¹²⁷ It however allows regulation to penetrate the inner workings of corporations and offers more transparency and potential engagement for stakeholders and civil society. This could make a stealthy inroad into the Anglo-American shareholder-centric corporate law model in the UK.

¹²⁴ Koen HM de Roo, 'The Role of the EU Directive on Non-Financial Disclosure on Human Rights Reporting' (2015) 12 *European Company Law* 278.

¹²⁵ Andrew Johnston, 'Reforming English Company Law to Promote Sustainable Companies' (2014) 11 *European Company Law* 63, in the Special Issue of the *European Company Law on Sustainable Companies*, 2014.

¹²⁶ Mark B Taylor, 'Due Diligence: A Compliance Standard for Sustainable Companies' (2014) 11 *European Company Law* 86.

¹²⁷ A range of company law options and reforms were canvassed in the Special Issue of the *European Company Law on Sustainable Companies*, Volume 11(2), 2014. A more comprehensive reform for sustainable companies is mooted in the Sustainable Companies Project that makes business and responsibility an integrated concept and operationalised in practice, see Beate Sjöfäll, 'Regulating Companies as if the World Matters: Reflections from the Ongoing Sustainable Companies Project' (2012) 47 *Wake Forest Law Review* 113.

