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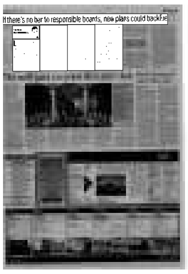

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If there's no bar to responsible boards, new plans could backfire

STEPHEN BARTHOLOMEUSZ

LAST month the Federal Government referred a proposal for a radical broadening of the concept of directors duties to its Corporations and Markets Advisory Committee. It is conceivable that the proposal could be embraced, probably for the wrong reasons, by directors and social activists

The Government has asked the committee (known as CAMAC) to consider the extent to which the duties of directors under the Corporations Act should include corporate social responsibilities or explicit obligations to take account of the interests of classes of stakeholders other than shareholders.

The referral is in part a response to controversies generated by the special committee of inquiry into James Hardie Industries' funding of asbestos victims and the bitter dispute that occurred between the company and victims.

If CAMAC were to recommend adopting a social overlay to existing directors' duties, it would threaten long-held convictions — and long-established legal precedent — that directors owe their duty to their company and, primarily, its shareholders. Or would it?

There is an international discussion occurring about whether the concept of directors' duties should be broadened, by statute or through voluntary codes, to include other stakeholder groups such as employees, suppliers, customers and the community and to take account of other factors, such as the environment.

Writing in *The Australian Financial Review* this week, the director of the Centre for Corporate Law and Securities Regulation at the University of Melbourne, Ian Ramsay, said that earlier this year the British Government presented a draft company law reform bill to Parliament that proposed incorporating a concept of "enlightened shareholder value" into directors duties.

Professor Ramsay said that under the British bill the primary duty of directors would still be to shareholders, but directors must take into account, where appropriate, the interests of other stakeholders. The proposal is that directors take into account the likely consequences of any decision for employees, suppliers, customers and others, and that they consider the impact of the company's operations on the community, environment and the company's reputation for high standards of conduct.

He said an earlier proposal that would have allowed directors to set the interests of other stakeholders above shareholders' was rejected, as it could have led to directors having more discretion and being less accountable for use of company resources.

In the wake of the Hardie saga, there have been calls for legislative responses to force companies to take account of other stakeholders and employees — although, ironically, Hardie's chairwoman, Meredith Hellicar, has herself argued for an expansion of directors' duties to include all stakeholders. She has said giving rights to other stakeholders would enable boards to feel more comfortable being generous with company funds beyond legal requirements: "What one needs is a safe harbour for directors to be able to integrate corporate social responsibility into their decision-making without fear that they are going to be sued both personally and as a company by their shareholders."

Hardie, under pressure, has agreed to direct a substantial proportion of its cash flow for the next 40 years to fund victims' claims. Where Hellicar sees reform providing protection for directors, social and environmental activists would see it as a green light to impose their agendas.

A basic question is whether companies are in practice constrained from considering a broader range of stakeholders. Hardie's own eventual acceptance of its responsibility for the victims suggests not. CSR has been making voluntary payments to asbestos victims for decades. Australian resource companies have become world leaders in adding a social responsibility dimension to their interaction with the communities

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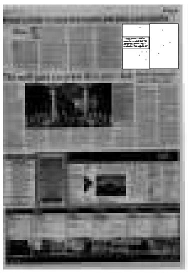

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within which they operate. Australian companies provided a torrent of cash for the tsunami appeals. Most Australian companies take the welfare and aspirations of their employees very seriously. Few could disregard the interests of their customers for any length of time.

‘A basic question is whether companies are constrained from considering a broader range of stakeholders. This suggests not.’

Plus, of course, there is a raft of specific legislation creating obligations and liabilities relating to employees, the environment and the community and, of course, the pressure of expectations from the communities that effectively provide companies with their licences to operate.

The fact that companies do more than the legal minimum for non-shareholder stakeholders says boards don't define their obligations narrowly.

That isn't surprising. There is an increasing understanding that it is good business — and good for the long-term interests of the company and shareholders — for companies to be good employers and good citizens. The damage done to Hardie, or that Ok Tedi did to BHP in a different era, provides graphic evidence of the reputational and financial consequences of defining shareholder interests too narrowly.

Adding layers of subsidiary obligations to directors' duties to their companies could also, oddly, require standards of behaviour from boards and companies — and impose liabilities — above those imposed by specific statutes. It would add complexity and confusion.

The development of socially responsible investment entities and research and triple-bottom-line reporting, plus the effect of case studies including Hardie, is increasing awareness and scrutiny of companies' treatment of non-shareholder stakeholders. The breadth of directors' fiduciary obligations has already been expanded.

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