

Final Corrected version (26th March 2009)
Respondent's comments (1900 words) by Peter Vass on:

Corporate Responsibility, Regulation and Partnered or Collaborative Governance

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In response I would like to offer some challenges to the idea of partnered or collaborative governance, in particular as set out by Prof Midttun, and to help answer the general question as to whether CSR (or CSER) as currently conceived can make a contribution, or is primarily a distraction.

I start by suggesting that partnership is a 'horizontal' concept, and may not do justice to the reality of the separate, and hierarchical, roles and responsibilities of government and business. My view is that a better understanding of their respective domains - and interfaces - will lead us to the necessary answers to tackle pressing social and environmental problems, ie, knowing 'who should do what, and why'.

There are four realms of governance that need to be addressed - and all four should be subject to debate, within their respective spheres of operation, about the principles and practices which need to be institutionalised and codified to help achieve better governance, and hence outcomes. These are:

- Policy governance: managing public risks
- Regulatory governance: managing public risks
- Corporate governance: managing business risks
- Personal governance: managing private risks

and we should note that a government's management of public risks 'encloses' the management of the other risks, given the definition of public risks as those risks, out of the set of all risks, which governments can legitimately adopt to manage on behalf of citizens (for more discussion on the development of this concept, see Bartle and Vass (2008), Risk and the Regulatory State - A Better Regulation Perspective, CRI Research Report 20, University of Bath, (downloadable www.bath.ac.uk/cri).

The way in which the better regulation agenda can be given effect was well set out by Christopher Clarke, Deputy Chairman of the Competition Commission, when describing the 'independent' regulatory role of the Competition Commission, and in his references to the work of bodies such as the Better Regulation Task Force (although governments have to be continually encouraged to have 'credible commitment' in this area, noting that the BRTF, and its successor bodies, the Better Regulation Commission (BRC) and the Risk and Regulation Advisory Council (RRAC), have all been abolished, leaving only the Better Regulation Executive (BRE) in the Dept of Business, Enterprise and Regulatory Reform (BERR)).

The benefits of institutionalisation and codification of good corporate governance principles and practices in relation to addressing business risks have clearly been given a renewed focus by the recent credit crisis and the conduct of the boards of directors of banks, as Professor David Parker observed, referring to 'corporate governance irresponsibility'.

Governments manage public risks arising from:

- Abuse of monopoly power
- Externalities
- Public goods arising from missing markets, inadequate standards or asymmetry of information
- Unacceptable distributional outcomes.

In this context we can reflect on the question put by Tom Todd of the European Commission: “Can business articulate a purpose beyond profit?”. It could, but perhaps it should not, given that it might not be legitimate, efficient, effective or sustainable. It can reasonably be said that the ‘business of business is business’ where public risks are effectively (and cost-effectively) managed by the regulatory state. And even where they aren’t, the objective should be to improve the performance of the regulatory and providing state, not seek its partial substitution by CSER in the corporate sector.

This issue of state and corporate responsibility is particularly important internationally, given the emphasis and expectations being placed on MNCs to take responsibility for issues which should properly be addressed and regulated by governments, both domestically and by international agreement. At present, NGOs, the UN and the OECD are taking on the role of quasi-governments in this field, but have to rely on global voluntary codes to encourage MNCs to self-regulate. This process may be a necessary one, given the variable state of development and government around the world, and problems such as child labour and corruption, but the end game should nevertheless be focused on achieving a wide spread of governments which are ‘good regulatory states’, within which the business of business can then be business.

To address the role of CSR, it is best unbundled as a subject into three parts to show its true scope and limitations. These are:

Corporate social irresponsibility (CSI): cutting corners on the minimum requirements and standards set by the regulatory state (the issue is therefore to ensure compliance).

Corporate social discretion (CSD): voluntarily setting standards higher than the minimum requirement set by the regulatory state, where there is a ‘business case’.

Corporate social misdirection (CSM): Directors allocate resources to social and environmental activities for which there is no business case (unless explicit permission has been sought from the owners to do so).

Professor David Parker refers to the idea of CSD in his introductory paper with Professor David Grayson (p7), citing the European Commission and the term “voluntary CSR”. However, we should note that the Commission documents in which this was developed went on to state clearly that voluntary CSR is predicated on a ‘business case’, and that CSR cannot substitute for the role of the regulatory state in setting due environmental and social standards (see for example, Communication from the Commission Concerning Corporate Social Responsibility: A Business Contribution to Sustainable Development, COM 2002, 347 final).

I think it is fair to say that most of the time that we hear governments exhorting business to focus on CSR, it is either, quite rightly, to point out to business that they should not be acting with CSI, or reminding them that there are business opportunities in higher standards (although the search for competitive advantage should seek those out in any event). An alternative cynical point is that it occurs when governments are trying to avoid their responsibilities to act ('tough decisions'), and so deflect attention by suggesting it someone else's role and responsibility. A clear example is action on climate change, where governments spend too much time exhorting companies and the public to address the problem for themselves, rather than focusing on the necessary role of government.

Understanding the separation, and respective roles and responsibilities, of government and business is very relevant to answering the key question put by Dr Zadek in his presentation: "What will it take to resolve the climate crisis?".

This is because it cannot be solved by companies and CSER alone. It is a collective action problem that has to be addressed by all governments together, which are required to set the control and incentive framework within which, and to which, companies and individuals will respond in delivering the controlled outcome cost-effectively. The traditional tools of economic and financial analysis are all that is necessary to guide policy makers and governments to the right solution. The line of argument would be as follows:

- There is a scarce resource: the ability of the global atmosphere to absorb CO₂eq emissions safely with respect to climate change.
- There is therefore a need for an international agreement by all nations to cap emissions (an externality) on a scientifically judged profile to 2050 and beyond.
- The marginal cost of the global CO₂eq cap (ie constraint) needs to be internalised into a 'price of carbon' affecting all supply chains, both domestic and international, such that all final consumer pay the full cost-reflective price for the CO₂eq emissions embedded in the goods and services supplied.
- The mechanism to achieve this is an international cap and trade system. Carbon taxes are an inappropriate instrument because they are a fixed price delivering an uncertain quantity, when what is required is a certain quantity (compliance with the global constraint) achieved through an adjusting price (the cost of emission certificates). Also, carbon taxes cannot be traded internationally, which is an essential feature for an equitable international agreement, and a cost-effective outcome.

The two key governance aspects of this analysis for tackling dangerous climate change are:

- 1.** An equitable allocation of initial allowances (ie, 'property rights') to emit CO₂eq to countries before trading (as this generates the necessary flows of money from developed to developing countries, and deals effectively with the 'historical legacy').
- 2.** Establishing an international carbon authority (ICA) and national carbon authorities (NCAs) in each country, organisations which would develop the framework for government auctions, trading in secondary markets, reporting, compliance and enforcement.

In such a scheme there is no need to set specific targets for CO₂eq reductions in each country. CO₂eq emitting organisations would decide on their carbon management strategy depending on whether they are better off buying emission certificates to back their emissions or to abate their emissions to avoid the cost of purchasing certificates. The price of carbon would incentivise both producers and consumers, as well as technical innovation. Government command and control policies aimed at particular technologies would not be required, and high transactions cost options, such as 'personal carbon trading' could be avoided by it being an 'upstream approach', ie fuel retailers to the domestic sector would have to back their sales with purchased emission certificates (for the full development of this framework, see Bartle and Vass (2007), Climate Change Policy and the Regulatory State, CRI Research Report 19, University of Bath (downloadable from www.bath.ac.uk/cri).

Conclusion

Such analysis leads me to the conclusion that the separate domains of government and business should address the institutionalisation and codification of the principles and processes of good governance relevant to their respective domains (to help reduce wholly 'avoidable' corporate or government failures). The interface between them would then be reflected in appropriate regulatory and statutory constraint on business, and the development of self-regulation by business with 'strategic' regulatory oversight. Examples of such supervised self-regulation include the Combined Code on Corporate Governance (2008) overseen by the Financial Reporting Council (FRC), industry broadcast standards overseen by Ofcom, and the control of BTs monopoly power in wholesale markets through the threat of regulatory intervention if fair, efficient, cost-reflective access prices are not maintained. There are many more examples. Such a perspective would help understand the problem referred to by David Parker and David Grayson on page 7 of their introductory paper (Robert Reich's point that CSR distracts opinion-formers from the proper task of influencing governments to act, and may dilute pressures for changing public policy).

In this respect many of you will remember the direct action campaign lobby, 'Camping for Climate'. Instead of camping out in front of BAA's headquarters at Heathrow, on this analysis they should have been camping on the steps of no 10 Downing Street! Also we saw clear evidence for the split of roles and responsibilities between government and business when business leaders in both the UK and the US went to Tony Blair and President Bush respectively to say that they would welcome government action to introduce a comprehensive cap and trade system (therefore still leaving a level competitive environment) because without it they recognised that their businesses, and business in general, would not be sustainable.

Two final points. First, I doubt that we should ascribe moral sentiments to wholly 'soulless' corporations (although we can demand that they give reasons for decisions, the accountability of which may force them to act with due morality). Secondly, I own up to being a systems rationalist.

Peter Vass
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