Parliamentary Joint Committee on Corporations and Financial Services
Rethinking national corporate regulatory systems in a global economy
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The regulatory challenge

1. In 1974 the Senate Select Committee on Securities and Exchange recommended that the national economy that had emerged required national regulation of corporations and securities markets. Labour, environmental and consumer standards now regulate business activity across Australia; however, their beneficial effect in preventing the externalization of social cost stops at its borders.

2. Over the past three decades, however, the economy has globalized—business, especially manufacturing, operations have moved offshore and trade, investment and currency flows have been thoroughly liberalized. Global production systems source components and locate stages of production to sites of lowest effective cost. Firms are part of supply chains operating as global networks crossing national boundaries. The components of these international production networks are highly mobile and relatively easily transferable. Price competition puts strong downward pressure on labour conditions and other social protections for workers and others affected by operations. The threat of investment flight to a more accommodating jurisdiction is a constant for developing countries. The mobility that globalisation gives to foreign direct investment, in the context of a competitive auction for investment capital, undermines host state capacity to enforce social protection and standards since these invariably impose costs for firms. Human rights problems are ubiquitous in the modern supply chains in which most levels of Australian business are engaged: few Australian companies today do not confront human rights problems.

3. There is no global regulatory mechanism for the new global economy; national regulation is all. Home states do not, with few exceptions, regulate the offshore operations and business relationships of their locally incorporated and headquartered firms; that responsibility is left to host states. The investment appeal of these host states—the relative poverty of their populations—is invariably matched by the poverty of their governance and social protection mechanisms, and perverse local incentives that militate against amelioration. The beneficial effects of our national regulatory are wholly absent from the production of the bulk of the consumer goods and many other products that Australians enjoy.

4. Investment liberalisation increases financial performance pressure upon managers. The threat of displacement by hostile takeover and pressure from institutional investors focused on financial return sharpens the profit focus. Institutionalization of investment adds a second level of fiduciary focus on financial return. It is fanciful to think that capital will protect labour and the environment—that is not its function; its incentives are otherwise.

5. Should this problem concern the committee? Consumers benefit from global supply chains even if at the cost of local jobs lost offshore. And offshore production is an undoubted boon to many of its workers, given the alternative of grinding poverty. Yet the considerations that ground our regulation of Australian firms—the freedom, dignity and social welfare of our citizens—do not end, as our regulation does, at national borders. They apply equally to all humanity. The challenge is to globalize our system of corporate responsibility and extend its beneficial effect to others affected by the operations and business relationships of our firms.

Options for globalizing corporate responsibility

6. Several options are available for doing so. I shall canvass some in what I judge to be the ascending order of feasibility and/or moral obligation.

7. There is currently a process in the UN Human Rights Council leading to consideration of a binding treaty on business and human rights. Support for the process is divided sharply along OECD membership lines: none of the 20 votes cast for the resolution in June 2014 came from OECD members and 12 of the 14 opposing the resolution were OECD adhering governments. Treaty ratification would, of course, be voluntary and a modest level of ratification might be anticipated from home states of major firms if the proposal led to a treaty. There are also formidable problems with such a treaty—the rigidity of its terms, effective implementation and enforcement.

8. The OECD might itself be the vehicle of collective action by developed states to extend the protection of their national systems. The OECD *Guidelines for Multinational Enterprises* are a voluntary standard of responsible conduct addressed to firms operating from and in these states; a mediation mechanism of uneven quality is provided through National Contact Points. Pressure from the United States, which had acted unilaterally in 1977 to criminalise corrupt corporate payments to foreign public officials, led to the OECD adopting a binding corruption convention in similar terms. There is no current movement in the OECD for prescriptive standards to replace the voluntary *Guidelines*.

9. Unilateral national action by a host state is another possibility. The US *Foreign Corrupt Practices Act* 1977 is the striking exception to the almost universal reluctance to regulate offshore corporate activity and relationships although in the UK the *Bribery Act 2010* and the *Modern Slavery Bill 2014* are recent further exceptions of specific application. In Australia, a predecessor committee to the PJC judged an Australian Democrats Bill to regulate offshore conduct of Australian firms to be "unnecessary and unwarranted".[39]

10. The United Nations has endorsed non-binding corporate responsibility standards that are claimed to enjoy wide business support. The Human Rights Council's 'Protect, Respect and Remedy' framework for business and human rights includes the pillar that all business enterprises have a responsibility to respect the human rights of those affected by their activities and business relationships (RtR). In 2011 the Council endorsed the *Guiding Principles on Business and Human Rights* (*Guiding Principles*) to operationalize the framework. A UN Working Group has been established to promote their implementation and the OECD *Guidelines* have been amended to include the responsibility to respect (RtR) standard.

11. The 'Protect' pillar of the *Guiding Principles* is directly relevant to legislators, regulators and oversight bodies of national corporate systems. Expressing international law principles, the pillar requires states to protect against human rights abuse within their territory by third parties, including business enterprises. It also requires states (and this obligation applies to home as well as host states) to set out clearly the expectation that all business enterprises domiciled in their territory respect human rights throughout their operations. In meeting their duty to protect, states should ensure that laws and policies governing the creation and ongoing

[39] Parliamentary Joint Statutory Committee on Corporations and Securities, Parliament of Australia, *Report on the Corporate Code of Conduct Bill 2000* (2001), [3.3], [4.4]-[4.6].

operation of business enterprises, such as corporate law, do not constrain but enable business respect for human rights. They should also provide effective guidance to business enterprises on how to respect human rights throughout their operations and should encourage, and where appropriate, require, business enterprises to communicate how they address their human rights impacts (*Guiding Principles* 1-3).

12. The *Guiding Principles* stress the importance of national corporate and securities law to promote the RtR and the difficulties often presented by national systems:

> *Laws and policies that govern the creation and ongoing operation of business enterprises, such as corporate and securities laws, directly shape business behaviour. Yet their implications for human rights remain poorly understood. For example, there is a lack of clarity in corporate and securities law regarding what companies and their officers are permitted, let alone required, to do regarding human rights. Laws and policies in this area should provide sufficient guidance to enable enterprises to respect human rights, with due regard to the role of the existing governance structures such as corporate boards.*
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> *Guidance to business enterprises on respecting human rights should indicate expected outcomes and help share best practices. It should advise on appropriate methods, including human rights due diligence, and how to consider effectively issues of gender, vulnerability and/or marginalisation, recognising the specific challenges that may be faced by indigenous peoples, women, national or ethnic minorities, religious and linguistic minorities, children, persons with disabilities, and migrant workers and their families.*

13. Australian corporate law needs be compatible with and, ideally, hospitable to the *Guiding Principles,* and not an impediment to their internalisation. Areas of significant concern include the following:
    - The scope of the licence under directors' duties to respond to the RtR when profit-sacrificing;
    - The separate legal entity principle and limited liability within corporate groups especially with respect to parent company responsibility for human rights abuses by subsidiaries and affiliates;
    - The entitlement of shareholders to raise RtR concerns at AGMs;
    - Clarification of financial reporting requirements concerning human rights impacts especially around standards of "materiality" or "significance" to the economic performance of the business enterprise; and
    - The corporate associations restrictions under takeovers law in exercise of the corporate responsibility to use leverage to prevent or mitigate adverse human rights impacts (cf Guiding Principle 19(b)(ii)).

    The writer hopes to canvass these concerns in discussion with the PJC.

14. A consensus resolution passed at the June 2014 session of the Human Rights Council specifically called on states to ‘take steps to implement the Guiding Principles, including by developing a national action plan or other such framework’. Australia was a signatory to this resolution. Denmark, the Netherlands and Britain have developed NAPs and draft plans are

in preparation in a number of other states. Australia has made no commitment to a plan and there appears no present appetite for one. That appears to be a lost opportunity.

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