

International Chamber of Commerce, Stockholm, 26 May 2010.

Transcript of luncheon speech by Claes Cronstedt, Gaemo Group, on corporate behaviour and increasing demands.

Ladies and Gentlemen,

Most corporate leaders have understood that CSR is important – but only a few know *what* they must do or what they are *allowed* to do. And there are many critics. Stefan Stern from Financial Times wrote last year: “*Thank goodness, now the recession’s there we can forget all that nonsense about CSR and get back to trying to make some money*”.

I have six important questions condensed into fifteen minutes.

1. *The borderline between voluntary and mandatory.*
2. *Importance of human rights and environmental due diligence.*
3. *Soft law and self-regulation initiatives.*
4. *Piercing the corporate veil?*
5. *Does the financial crisis impact on CSR?*
6. *The future of CSR.*

1. The borderline between voluntary and mandatory. In spite of the Universal Declaration of Human Rights and the many conventions that followed on e.g. discrimination, torture, children’s and women’s rights, approx four billion people live outside of the rule of law according to a recent UN report. Virtually every component of the justice system, police, defence lawyers, prosecutors, and courts, works against, not with, the poor in providing the protection of the law. This enforcement gap has also disastrous effects on economic productivity and stability and fuels corruption on all levels. It also benefits free riders; those businesses that earn money through unfair competition by violating human rights and harming the environment with little risk of being held accountable.

It is the structural inequalities and power imbalances in the world that have created

CSR. Some argue that CSR is only the voluntary standard setting beyond compliance. But when mandatory law is dysfunctional or lacking - what happens? CSR expands. The reasoning is the following. Companies are expected to comply with local laws even if they are not enforced in practice. If national law is unsatisfactory or absent, the principles in relevant international instruments shall be respected. If national law violates human rights, such as apartheid, the situation gets more complicated and that's another story. However, in short what the company is not allowed to do at home, it must not do in the host country either. Hence, broadly speaking it could be argued that CSR in practice is mandatory. The consequence is that the multinational corporations 'export' application of international norms on human rights and environment to developing countries; and thus reduce the enforcement gap. Perhaps you can call it a *lex Mercatoria* process (soft rules that crystallizes to hard law - 'belief' arises from custom).

2. Importance of human rights and environmental due diligence. Professor John Ruggie, Harvard Law School and the Special Representative of the UN Secretary General on human rights and transnational corporations and other business enterprises was referred to in Financial Times, 30 December 2009: *"He admits to being surprised at, even at this late date, how little the headquarters [of many companies] actually know about what is happening on the ground in difficult regions. Rare is the company with really good due diligence systems that has the ways of dealing proactively with concerns of the local community"*.

Ruggie points out the risk of being accountable for violations of human rights committed by someone else, such as a repressive government or a joint venture partner. It is called complicity. An in-depth due diligence reduces the risk for the company to enter a zone of legal danger of being complicit of human rights abuse. The management must initially consider e.g. the following before an investment or cooperation is further discussed:

- Do we have information about any risk, that gross human rights abuses might occur in a particular situation; e.g. information from our own sources, from experts, NGO's, media, Internet?

- Do other actors involved in the project or situation have a track record of human rights abuses?

- Have we taken precautionary measures to minimise the risk of harm? Are they the kind of measures that a careful, responsible company would have taken?

Although human rights due diligence is a natural extension of a company's risk management, it is unique in several respects. It is not a one-time transaction activity but an ongoing process. The requirements of conducting a careful due diligence have increased in the past five years. There are around 50 lawsuits in the US against corporations that are claimed to have been complicit in human rights abuses outside the US. Most of these defendants have failed to do their due diligence home work. As John Ruggie puts it: *"Human rights due diligence can be a game-changer for companies from 'naming and shaming' to 'knowing and showing'"*.

3. Soft law and self-regulation initiatives. Adherence to so-called 'soft law' initiatives such as the ILO Tripartite Declaration, OECD Guidelines and self-regulation such as the UN Global Compact and company codes are effective ways to create levelled playing fields also to the benefit of human rights and environment. The Kimberly Process Initiative (conflict diamonds), the Extractive Industries Transparency Initiative and the Equator Principles (banks) are fine examples. E.g. the participating banks will not provide loans to projects where the borrower will not or is unable to comply with the organisation's social and environmental policies and procedures that implement the Equator Principles.

Companies that do not adhere to a soft law initiative or are not a 'member' of a collective self-regulation initiative may find it difficult to compete in public procurement processes or to be included in World Bank finance programs and, sooner or later, are generally becoming an unwelcome business partner. Hence, do not underestimate soft law; by joining an initiative the company undertakes to follow

certain good standards and is considered trustworthy - and it indirectly contributes to the enforcement of the rule of law. There are rising expectations that solutions to reduce the enforcement gap will come from business and that national lawmakers will follow suit. Such expectations will put business increasingly in the spotlight.

4. Piercing the corporate veil. An incorporated subsidiary does not guarantee safety from liability for the parent company. So far the legal concepts of the strict corporate separate legal personality and related limited liability are like stonewalls, and as old. It is called *the corporate veil*. A multinational corporate group can consist of myriads of subsidiaries, many of which do what the parent company tells them to do. In spite of that, only the violating subsidiary can be held accountable, while the parent generally is legally 'untouchable'. To try to *pierce the corporate veil* presents significant difficulties to those victims seeking justice. But this may change. A tougher climate is evolving; to protect the poor is to create stability, which is good for business. As the Harvard Business School Professor Michael Porter writes: "*Successful corporations need a healthy society*". Ongoing discussions suggest that a corporate group would, in cases of human rights and environment abuses, be considered as one entity, similar to tax and competition acts. This means that the parent company, with the deep pocket, can be held accountable.

5. The financial crisis impact on CSR. Is Stefan Stern right that we can forget about all that nonsense about CSR, now, as we have the financial crisis? No, on the contrary: national regulations prove to be insufficient to steer global markets and international standard setting as on the G 20 level is burdened and slowed down by national interests and compromises. Therefore the soft law and best practice standards of CSR could offer a swift and flexible solution to ban certain practices, which proved to be detrimental to the economy and the society at large. And CSR has no political implications. Then we have the 'Main Street' that claims that CSR is more important than ever - if the bankers are unreliable why should the corporate leaders be different, they say.

To make it work CSR must be embedded in the corporate culture, strategy and

governance systems. Corporate culture is a concept in corporate governance and CSR, which is more and more talked about, specifically since the financial crisis. In short, the corporation shall show that it has a culture that has emerged from a decision making process, recognized as authentic and authoritative within the corporation that encourages ethical conduct within its organization. Does this mean that the successful CEO has a high EQ?

Where is CSR heading? Towards stricter standard setting and enforcement. Those who violate human rights and harm the environment must be punished stiffly, it is said. The Siemens corruption case shows how fast society is changing. Ten years ago bribes paid in foreign countries were tax deductible in Germany as business expenses. The Siemens management had obviously not taken serious that the general attitude concerning bribery had undergone a fundamental change. The case hit Siemens hard: the share price went down significantly in addition to the approx two billion Euros in fines, attorneys' fees, cost for the implementation of a new compliance scheme, the exchange of the top management etc.

BHP Billiton, the world's biggest miner admitted some weeks ago that it had uncovered possible corruption involving the bribery of foreign government officials at some of its exploration projects. BHP is the latest in a series of multinationals whose dealings in foreign markets have come under scrutiny as international regulators step up their efforts to tackle corporate corruption. Last month, four employees of Rio Tinto were jailed in China after admitting taking bribes.

BBC reported this month that the British publisher Macmillan is facing a six-year ban from taking up any contracts financed by the World Bank. The move comes after Macmillan admitted making bribery payments to secure a deal to print textbooks in South Sudan.

There are class actions pending in a New York court against fifty corporations and banks that operated in South Africa during apartheid. The plaintiffs claim 400 billion USD in damages alleging that the defendants, by doing business with the apartheid-

era government, were complicit in gross violation of human rights. There are around 50 cases in the US against corporations concerning alleged complicity.

There are many more examples and lawyers are catching the trend and are dipping into the growing body of international human rights and environmental concerns, to find new ways of arguing cases for victims. We lawyers are relying on the old dictum that sometimes you have to start a fight to discover how to win it. Hence, corporate leaders are facing new challenges. They should not kick the can down the road. CSR is growing more and more and becoming stiffer because people care about social justice and the environment in a troubled world.

Mr Carl Henric Svanberg, the beleaguered chair of BP - when he finally made a statement about the oil disaster - he said (translation): "*Safety must come first. That is also logical - in the end a failure cost much more than what you may have saved*". Already the old Greeks knew that 'prevention is better than cure'.

/Thank you.

<http://www.gaemogroup.com>

