

**BOARDROOM WARMING – A ROLE FOR COMPANY  
DIRECTORS IN CLIMATE CHANGE MITIGATION**

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This thesis is presented for the Honours degree of Bachelor of Laws of Murdoch  
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## ABSTRACT

*Current climate change mitigation policy has been entirely ineffective in bringing about a reduction in greenhouse gas emissions. The adoption of a top down management approach combined with an over reliance on environmental law principles indicates that policy makers have failed to understand the unique nature of the climate change problem. Climate change is a 'wicked' problem – it does not respond to the top down and internationally focused approaches currently employed. Further, our approach to managing climate change and its impact is dependent on our understanding of the problem at any given time. This is particularly problematic with climate change as our understanding of its likely impacts and how we respond to them shifts rapidly. Climate change and the governance of climate change are complex and difficult issues involving many parties. Negotiations around national and international climate change policy must take into account a wide range of interests and have become more complex due to the increased role of non-state parties. It is argued here that forms of governance that work at a lower level and embrace the participation of non-state actors such as corporations are more effective in dealing with wicked problems such as climate change.*

*Despite the fact that corporations are among the largest greenhouse gas emitters and are responsible for almost all significant environmental outcomes, their potential to play a key role in climate change mitigation has been largely ignored. This essay proposes that the impact of climate change would be better managed by a bottom up approach that incorporates corporations and their directors as key decision makers. It is proposed that the best way to do this is by the introduction of a new directors' duty that requires company directors to take into account the interests*

*not only of shareholders, but also of future generations and the climate itself. Principles of intergenerational and intragenerational equity and stakeholder theory are called upon to inform this new approach. These theoretical tools allow for the development of a model that accommodates several stakeholders while still preserving the economic benefits brought by incorporation. Corporate social responsibility initiatives and separate legislation are examined and found wanting as alternative methods for incorporating corporations into a bottom up approach to climate change mitigation. It is argued that directors' duties, because of their established legitimacy, wide acceptance and well understood enforcement mechanisms are the ideal legal tool for the job. Under the current law, directors face uncertainty about how far they can go in acting in the interests of stakeholders other than shareholders. It could even be said the current law creates a disincentive to divert corporate resources to reducing a corporation's greenhouse gas emissions. It is argued here that a new duty that imposes an obligation on company directors to take into account the interests of shareholders, the climate and future generations will remove uncertainty and allow corporations to meaningfully participate in a bottom up approach to effective climate change mitigation.*

## I INTRODUCTION

Climate change is not so much a problem of changing weather patterns as it is of governance. To date, none of the instruments developed to mitigate climate change have been effective.<sup>1</sup> This is because they were, by their very design, never capable of dealing with the type of problem presented by climate change. The instruments developed to deal with climate change were based on policies which in the past had been used to deal with problems such as ozone depletion, acid rain and nuclear disarmament. Policy makers failed to realise that climate change is entirely different in nature to these other problems, and that any analogies between them were structurally unsound. It is argued in this essay that corporations have real potential to play a critical role in a new, bottom up approach to effective climate change mitigation. Key to developing this potential is the introduction of a new directors' duty to take into account the interests of shareholders as well as the climate and future generations.

Part II of this essay uses the 'wicked-tame' problem dichotomy first developed by Horst Rittel and Melvin Webber<sup>2</sup> to examine the unique nature of the climate change problem. Reasons why current climate change mitigation regimes have failed are also examined. Part III argues for a bottom up approach to climate change mitigation. It advocates a new, 'clumsy' approach as described by Gwyn Prins, Steve Rayner and Marco Verweij. Clumsy governance consists of a variety of actors, each

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<sup>1</sup> Gwyn Prins and Steve Rayner, *The Wrong Trousers: Radically Rethinking Climate Policy* (Joint Discussion Paper, James Martin Institute of Science and Civilization, University of Oxford and the MacKinder Centre for the Study of Long Wave Events, London School of Economics 2007) 8-13; Gwyn Prins et al, *The Hartwell Paper: A New Direction for Climate Policy After the Crash of 2009* (Discussion Paper, Institute for Science, Innovation and Society University of Oxford and London School of Economics MacKinder Programme for the Study of Long Wave Events, 2010) 15-16.

<sup>2</sup> Horst W J Rittel and Melvin M Webber, 'Dilemmas in a General Theory of Planning' (1973) 4 *Policy Sciences* 166, 160-167.

operating in different realms, at different levels and with different types of policy instruments.<sup>3</sup> Such an approach to climate change would recognise the diminishing role and authority of nation states in the governance of global issues such as climate change.<sup>4</sup> It is argued that by virtue of the power they hold, company directors have the potential to become a vehicle for effective climate change mitigation policy. A new directors' duty that compels directors to take into account the interests of the climate and future generations as well as shareholders is proposed.

Part IV positions the corporate form as a social construct, and examines different interpretations of what a corporation's purpose should be. This part commences with a brief history of the limited liability corporation and the doctrine of separate entity. The reigning economic theory of firm organisation is discussed, and an alternative, stakeholder theory, is introduced briefly. The conflict between shareholder primacy enshrined in corporate law and society's expectations of the social role of corporations is discussed.

Parts V and VI discuss the theoretical foundation of the bottom up approach proposed in this essay. Stakeholder theory and intergenerational equity respectively are called upon to inform this new approach to climate change mitigation. Stakeholder theory recognises that corporations' survival depends on the support of groups other than shareholders.<sup>5</sup> It is shown that the climate is a stakeholder which can have enormous impact on corporations. Intergenerational equity is the principle

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<sup>3</sup> Gwyn Prins and Steve Rayner, above n 1, 26-27; Marco Verweij et al, 'Clumsy Solutions for a Complex World: The Case of Climate Change' (2006) 84(4) *Public Administration* 817; Marco Verweij, 'Is the Kyoto Protocol Merely Irrelevant, or Positively Harmful, for the Efforts to Curb Climate Change?' in Marco Verweij and Michael Thompson (eds), *Clumsy Solutions for a Complex World: Governance, Politics and Plural Perceptions*, Global Issues (Palgrave Macmillan, 2011) 31, 41-44 53-55.

<sup>4</sup> Maarten Hajer, 'Policy Without Polity? Policy Analysis and the Institutional Void' (2003) 36(2) *Policy Sciences* 175, 175.

<sup>5</sup> R Edward Freeman, *Strategic Management: A Stakeholder Approach* (Pitman Publishing Inc, 1984).



that future generations have rights to access and enjoy the Earth's natural resources in the same capacity as present generations.<sup>6</sup> Because of their ongoing nature and their impact and dependence on the Earth's natural resources, corporations have an important and self-interested role in ensuring intergenerational equity.

Directors' duties are identified as an appropriate legal tool to assist in climate change mitigation because they are a proven and accepted mechanism for ensuring corporations fulfil their side of the social bargain entered into upon incorporation. By setting standards of behaviour, directors' duties play an important role in ensuring the benefits of incorporation flow freely and fairly. However, there are costs inherent in this mode of firm organisation. Part VII examines the problems brought by incorporation, and how directors' duties are used to mitigate these. These problems are mainly to do with the risks that come with separating company ownership and control. Under the current law, while a director could be found to have breached his or her duties by failing to take steps to protect the corporation from foreseeable climate change related harm, they would unlikely be found to be in breach simply because their company was not actively contributing to a reduction in greenhouse gas emissions. This means there is no incentive to do so, and even a direct disincentive in the form of not wanting to divert corporate resources away from shareholders and risk breaching their duty to act in the best interests of the company. This is why a new duty that does impose such an obligation is required if corporations are to form a key part of a new, bottom up approach to mitigating climate change. An effective and innovative way of achieving this is to make the climate itself and future generations the subject of the duty.

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<sup>6</sup> Edith Brown Weiss, *In Fairness to Future Generations: International Law, Common Patrimony and Intergenerational Equity* (The United Nations University, 1989).

Part XIII discusses corporate social responsibility and its role in tempering the impact of corporations on wider society. While the widespread adoption of corporate social responsibility practices in relation to climate change mitigation is acknowledged,<sup>7</sup> it is argued that due to their voluntary nature corporate social responsibility measures on their own are inadequate to effectively address climate change. Reasons why stakeholder theory is superior to corporate social responsibility in the context of climate change mitigation are discussed.

Part IX addresses why directors duties have been identified as the regulatory tool of choice. It puts forward a business case for company directors to take action to mitigate climate change due to the potentially disastrous effects climate change can have on a business. Directors' duties are essentially a mechanism by which parliament controls corporate impact on wider society. They work to ensure the benefits of incorporation flow freely and fairly. This part examines similar provisions in the *Companies Act 2006* (UK). Critiques of these provisions and other more general arguments against using directors' duties to further social goals are addressed. Enforcement paths, standing requirements and safe harbour provisions are discussed.

Climate change is a problem that corporations have largely contributed to and one which now affects everyone. In this light, harnessing the power of companies and their directors to play a role in climate change mitigation is fair and logical. The

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<sup>7</sup> See, eg, Investor Responsibility Research Centre, 'Corporate Governance and Climate Change: Making the Connection' (Research Paper, Ceres, 2006) <<http://www.ceres.org/resources/reports/corporate-governance-and-climate-change-2006/view>>; Ans Kolk, Jonatan Pinkse, 'Market Strategies for Climate Change' (2004) 22(3) *European Management Journal* 304; Shameek Konar and Mark A Cohen, 'Does the Market Value Environmental Performance?' (2001) 83(2) *The Review of Economics and Statistics* 281; Andrew J Hoffman, 'Climate Change Strategy: The Business Logic Behind Voluntary Greenhouse Gas Reductions' (2005) 47(3) *California Management Review* 21, 22-38.

proposed duty allows corporations to participate meaningfully in effective climate change mitigation and still pursue a profit goal, ensuring that the important benefits of incorporation are not lost.

## II WICKED PROBLEMS AND THE WRONG GOVERNANCE

Decades of summits, negotiations, conventions and agreements have failed to produce a single instrument effective in mitigating and preventing climate change.<sup>8</sup>

The reason is not that climate change is a problem too big or too complex, but that the solutions implemented were simply never going to be capable of dealing with the new and unique challenges presented by climate change.

The two main international instruments for climate change mitigation, the Kyoto Protocol and the United Nations Framework Convention on Climate Change (UNFCCC), failed for the same reasons: Both were children ill-conceived of a top down approach to governance and a misguided reliance on environmental law principles. As a result, neither instrument has achieved a reduction in greenhouse gas (GHG) emissions.<sup>9</sup> In fact, since their inception in 2005 and 1997 respectively, GHG emissions have increased. Further, neither instrument was enforceable. While of course the various emissions trading schemes (ETS)<sup>10</sup> designed to reduce GHG emissions by imposing a price on these emissions are established by domestic legislation and enforceable, other instruments such as the Kyoto Protocol are not, despite claiming to be. For example, when it became clear that Canada would breach its obligations under the Kyoto Protocol, rather than suffer censure, it simply announced it would not participate in a second Kyoto Protocol commitment period. No penalty followed this announcement and effective withdrawal from the treaty.<sup>11</sup>

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<sup>8</sup> Gwyn Prins and Steve Rayner, above n 1, 8-13; Gwyn Prins et al, above n 1, 15-19.

<sup>9</sup> Gwyn Prins and Steve Rayner, above n 1, 4.

<sup>11</sup> Hari M Osofsky and Lesley K McAllister, *Climate Change Law and Policy* (Wolters Kluwer Law & Business, 2012), 211.

### *A Problem 1: A Top Down Approach*

Both the UNFCCC and the Kyoto Protocol borrowed heavily from governance models previously used to tackle the problems of acid rain, ozone depletion and nuclear disarmament. It was not unreasonable for the officials tasked with negotiating a treaty to address climate change to take up these models as incremental adaptation from past successes is the norm in such negotiations. However, the analogies of these past problems with that of climate change, while superficially plausible, were structurally unsound and not applicable in the way the drafters assumed.<sup>12</sup> This was because the problems of sulphur emissions and nuclear bombs, while serious and complex, were nevertheless ‘tame’ problems. Rittel and Webber used this term to describe a type of problem for which it is clear when a solution has been found.<sup>13</sup> In each of the examples mentioned above, there were only a few causes of the particular harm, the causes were all identifiable and solutions were relatively simple and inexpensive to implement. Importantly, it was obvious when a solution had been reached and implemented.

Climate change, on the other hand, is a ‘wicked’ problem – a problem characterised by the impossibility of giving it a definitive formulation. Rittel and Webber defined this type of problem as one that is impossible to formulate definitively because the information required to understand it is dependent upon one’s idea for solving it.<sup>14</sup> Furthermore, it is impossible to know when a sufficient level of understanding of the problem has been attained, and the search for more knowledge and understanding can be stopped. Rittel and Webber also identified how wicked problems are characterised by having many parties equally equipped, interested and entitled to

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<sup>12</sup> Gwyn Prins et al, above n 1, 15.

<sup>13</sup> Horst W J Rittel and Melvin M Webber, above n 2, 160-167.

<sup>14</sup> Ibid.

judge the solution, but none who have the power to set formal rules to determine the correctness or quality of the solution.<sup>15</sup>

It is easy to see how climate change is a wicked problem. It is so much more than changing weather patterns and rising sea levels. Climate change is just one part of a larger complex of conditions affecting humanity. These encompass population, technology, economy and production, land and resource use, wealth disparities, and environmental justice. The scientific knowledge required to understand climate change and its causes and effects is dependent on how one believes it should best be dealt with.<sup>16</sup> For example, if one believes that adaptation is the best way to mitigate the effects of climate change, the knowledge sought out will be different to that sought if one believes that prevention is the best approach. There are also literally millions of state and non-state parties interested in the solution, and not one with the authority to implement a single global solution. These conditions have led some to say climate change is better understood as a persistent condition that can only be coped with and managed, not fixed.<sup>17</sup>

### *B Problem 2: Over Reliance on Environmental Law Principles*

Climate change policy has drawn heavily on other areas of legal scholarship, particularly that of environmental law. The link with environmental law is in fact so strong that the burgeoning body of climate change law has even been treated by some as a sub-specialty of environmental law.<sup>18</sup> As a result, the established environmental law principles of intergenerational equity, polluter pays, the

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<sup>15</sup> Ibid.

<sup>16</sup> Ibid.

<sup>17</sup> Mike Hulme, *Why We Disagree About Climate Change* (Cambridge University Press, 2009) 359-364.

<sup>18</sup> Jacqueline Peel, 'Climate Change Law: The Emergence of a New Legal Discipline' (2008) 32 *Melbourne University Law Review* 922, 923.

precautionary principle, common but differentiated responsibility and general notions of responsibility and prevention have coloured the development of international climate change instruments and domestic climate change law.<sup>19</sup> On its face, the close relationship between these two bodies of law seems intuitive and sensible: Both areas deal with the natural physical environment we live in, and both aim to preserve and protect this environment from damage caused by human activity. Also, these principles were developed to accord with ideas of equity and justice which, although not directly addressed in this essay, are both cause for significant concern in the climate change context.<sup>20</sup> However, closer examination of the types of issues that environmental law and climate change law serve to address reveals flaws in this approach. The types of problems these two bodies of law are designed to solve are fundamentally different: Environmental law is designed to address tame problems such as contaminated sites and air pollution. Climate change is a different kind of problem entirely and does not respond to regulation designed for tame problems.

Not only does climate change bring the challenges of empirical understanding found in any open system where the inputs are many and varied, it does so with unique spatial and temporal dimensions which transcend the limits of industrial risks of the past.<sup>21</sup> The sources and experiences of climate change risk are ‘indeterminately distanced over space and time, stretching social and natural relations of cause,

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<sup>19</sup> See, eg. Rowena Maguire, ‘Incorporating International Environmental Principles into Future Climate Change Instruments’ (2012) 2 *Carbon Climate Law Review* 101.

<sup>20</sup> For a discussion on how notions of equity and justice permeate the climate change debate, see, eg. Rosemary Lyster, ‘Towards a Global Justice Vision for Climate Law in a Time of ‘Unreason’’ (2013) 4(1) *Journal of Human Rights and the Environment* 32; Mark Stallworthy, ‘Environmental Justice Imperatives for an Era of Climate Change’ (2009) 36(1) *Journal of Law and Society* 55; Rowena Maguire and Bridget Lewis, ‘The Influence of Justice Theories on International Climate Policies and Measures’ (2012) 8(1) *Macquarie Journal of International and Comparative Environmental Law* 16; Jeremy Baskin, ‘The Impossible Necessity of Climate Justice?’ (2009) 10 *Melbourne Journal of International Law* 424; Sujatha Byravan and Sudhir Chella Rajan, ‘The Ethical Implications of Sea Level Rise Due to Climate Change’ (2010) 24(3) *Ethics and International Affairs* 239; Achala Chandani, ‘Distributive Justice and Sustainability as a Viable Foundation for the Future Climate Regime’ (2007) 2 *Carbon and Climate Law Review* 152.

<sup>21</sup> Matthew Gandy, ‘Rethinking the Ecological Leviathan: Environmental Regulation in an Age of Risk’ (1999) 9 *Global Environmental Change* 59, 59-60.

effect and responsibility.’<sup>22</sup> In other words, the climate is everywhere and so are the causes and effects of its changes. These changes and the risks they bring are unlike any changes humanity has had to address in the past, and new tools are required to understand and respond to them. Sheila Jasanoff lyrically describes the temporal and special dimensions of climate change and the challenges they present as being ‘...unbounded... everywhere and nowhere and hence not easily accessible to imaginations...’<sup>23</sup> Climate change forces us to consider periods of time not easily assimilated into the rhythms of human life cycles. Human beings are accustomed to circadian and seasonal rhythms of days and years. This makes information dealing with the longer spans of time the impact of climate change covers difficult to access and understand. This in turn makes developing policies that effectively manage climate change very challenging.<sup>24</sup>

The spatial dimension of climate change is a new problem for governance. Unlike ‘traditional’ environmental problems that have local causes and local effects, climate change manifests in local problems with global causes. To wit, a polluted river usually has a local cause – a factory pumping waste into it, or chemical runoff from nearby agriculture activities. Rising sea levels that imperil low lying islands, however, are caused by emissions emanating from all over the world. Alexander Zahar, Jacqueline Peel and Lee Godden use the term ‘global-global’ to describe the problems brought about by climate change.<sup>25</sup> This phrase captures well the unbounded spatial dimension of climate change. It also highlights the jurisdictional

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<sup>22</sup> Harriet Bulkeley, ‘Governing Climate Change: The Politics of Risk Society?’ (2001) 26(4) *Transactions of the Institute of British Geographers* 430, 432.

<sup>23</sup> Sheila Jasanoff, ‘A New Climate for Society’ (2010) 27(2-3) *Theory, Culture and Society* 233, 237.

<sup>24</sup> Issachar Rosen-Zvi, ‘Climate Change Governance: Mapping the Terrain’ (2011) 2 *Carbon Climate Law Review* 234, 235-237, Gwyn Prins et al, above n 1, 15-61; Gwyn Prins and Steve Rayner, above n 1, 13-14.

<sup>25</sup> Alexander Zahar, Jacqueline Peel and Lee Godden, *Australian Climate Law in Global Context* (Cambridge University Press, 2013), 12-14.



challenges this dimension of climate change brings. Who is responsible for fixing the problem we all contribute to? For it is not just big businesses that emit GHG, but every individual too.

### *C Problem 3: Lack of Enforcement*

Many commentators have identified reasons why the Kyoto Protocol has failed to achieve its goal of reducing GHG emissions and mitigating climate change.<sup>26</sup>

According to Scott Barrett a treaty requires three features to be successful. First, it must attract broad participation as an instrument that applies to some and not others will lack legitimacy and authority. Second, it must ensure compliance via real and unpalatable penalty. Last, it must do both these things while asking parties to change their behaviour.<sup>27</sup> On the first point, China, India and the USA, three of the world's four largest GHG emitters are not participants, significantly reducing the incentive for other participants to make concerted efforts to reduce emissions. Secondly, the treaty's enforcement mechanisms are so weak that nations can ignore their reduction obligations 'with impunity.'<sup>28</sup> When it became clear that Canada was going to exceed its emissions targets it simply withdrew from the treaty without sanction. Finally, questions about whether reported reductions are true reductions abound. For example, in order to induce them to sign the treaty, Japan, Canada and Russia were allowed to count preservation of existing trees and soil towards their reduction goals – hardly an effective way of reducing emissions, as these countries had harboured no plans to cut their forests or disturb their soil in the first place.<sup>29</sup>

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<sup>26</sup> See, eg, Gwyn Prins and Steve Rayner, above n 1, 8-13; Gwyn Prins et al, above n 1, 15-19, Mike Hulme, above n 17, 289-297.

<sup>27</sup> Scott Barrett, 'Climate Change Negotiations Reconsidered' (Briefing Paper for Policy Network, 2008) 2 <[http://www.policy-network.net/publications\\_detail.aspx?ID=2186](http://www.policy-network.net/publications_detail.aspx?ID=2186)>.

<sup>28</sup> Mike Hulme, above n 17, 296.

<sup>29</sup> Marco Verweij et al, above n 3, 34-35.

Borrowing from the treaty regimes used to tackle tame problems led to climate change policy that simply could not accommodate the wicked nature of climate change. The analogies used to develop the main instruments of climate change policy were structurally unsound,<sup>30</sup> and not applicable in the way the drafters assumed them to be.<sup>31</sup> In addition, they were not meaningfully enforceable. This misunderstanding of the climate change problem led to a fundamental framing error: Climate change was represented as a conventional environmental ‘problem’ capable of being ‘solved’ by conventional means when it is neither.<sup>32</sup>

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<sup>30</sup> Horst W J Rittel and Melvin M Webber, above n 2, 160-167; Steve Rayner, ‘Wicked Problems: Clumsy Solutions – Diagnoses and Prescriptions for Environmental Ills’ (Speech delivered at the James Martin Institute for Science and Civilisation Jack Beale Memorial Lecture on Global Environment, University of New South Wales, Sydney, July 2006)

<<http://www.sbs.ox.ac.uk/centres/insis/Documents/jackbealelecture.pdf>>.

<sup>31</sup> Gwyn Prins et al, above n 1, 15.

<sup>32</sup> Ibid.

### III THE CASE FOR A BOTTOM UP APPROACH

#### *A Polycentricism and Silver Buckshot*

In their seminal work, *The Wrong Trousers*, Prins and Rayner discuss in detail the reasons why the Kyoto Protocol in particular could never work as intended.<sup>33</sup> In addition to noting the problems discussed above, they point to the difficulties associated with multi-party negotiations at the nation state level. They argue the case for dealing with climate change at the lowest levels of decision making, including city councils and corporations. They stress the importance of moving away from the current top down, command and control approach and instead harness ‘the only driver of ...political action that has demonstrated reliability, namely self-propelled, enlightened self interest.’<sup>34</sup> It is this essay’s thesis that imposing on company directors a duty to take into account the interests of the climate and future generations is a way to harness this enlightened self interest. Company directors are directly incentivised to drive wealth creation for shareholders, and are limited only by legal restrictions on their behaviour. Corporations are responsible for by far the most GHG emissions. A duty requiring corporations (via their directors) to behave with a long-sighted, enlightened self interest would be an effective and cost-effective way to develop a bottom up approach to climate change

This ‘bottom up’ approach to policy development and decision making has been recognised as an effective way to deal with the wickedness of climate change.<sup>35</sup>

Elinor Ostrom explores the reasons why conventional theories of collective, state-led action appeared on the surface to be relevant, but, like many things to do with

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<sup>33</sup> Gwyn Prins and Steve Rayner, above n 1, 8-13.

<sup>34</sup> *Ibid.*, 10.

<sup>35</sup> Elinor Ostrom, ‘A Polycentric Approach for Coping with Climate Change’ (Background Paper to the 2010 World Development Project - Policy Research Working Paper 5095, 2009) 32-39; David H Cole, ‘From Global to Polycentric Climate Governance’ (2011) 2 *Climate Law* 395, 406-411.

climate change, were in fact an inappropriate means of mitigation.<sup>36</sup> Central to Ostrom's thesis is the recognition that complex, multi-level solutions are best for solving complex, multi-level problems, and that a polycentric, bottom up approach is just such a solution.<sup>37</sup> Others have called this a 'clumsy' form of governance, that is, a management approach that consists of a variety of approaches, each operating in different realms, at different levels and with different types of policy instruments.<sup>38</sup> Prins and Rayner coined the term 'silver buckshot' when arguing the case for clumsy governance,<sup>39</sup> alluding to the problems associated with the single silver bullet approach that is the Kyoto Protocol.<sup>40</sup> These commentators all make the point that global solutions negotiated at a global level, if not backed up by a variety of efforts at national, regional and local levels, are not guaranteed to work effectively.<sup>41</sup> Daniel Cole has even gone so far as to declare that these global solutions are 'virtually doomed to fail.'<sup>42</sup>

Cole points to several flaws in the existing global climate governance regime that result from a top down approach. He turns to the work of Jouni Paavola to frame governance as a function which should not be limited to the state,<sup>43</sup> and acknowledges the role of non-governmental organisations, including corporations, in governing resource use.<sup>44</sup> In this sense, governance can be seen as a continuum between state-based solutions and solutions championed by non-state actors, with

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<sup>36</sup> Elinor Ostrom, above n 35, 32-39.

<sup>37</sup> Ibid, 38.

<sup>38</sup> Mike Hulme, above n 17, 309-317; Marco Verweij et al, above n 3; Marco Verweij, above n 3, 53-55.

<sup>39</sup> Gwyn Prins and Steve Rayner, above n 1, 26-27; Steve Rayner and Gwyn Prins, 'Time to Ditch Kyoto' (2007) 449 *Nature* 973, 974.

<sup>40</sup> Gwyn Prins and Steve Rayner, above n 1, 26-27; Steve Rayner and Gwyn Prins, above n 39, 974.

<sup>41</sup> See especially Elinor Ostrom, 'Nested Externalities and Polycentric Institutions: Must We Wait for Global Solutions to Climate Change Before Taking Action at Other Scales?' (2010) 49(2) *Economic Theory* 353; David H Cole, above n 35, 406-411; and Angela Oels, 'Rendering Climate Change Governable: From Biopower to Advanced Liberal Government?' (2005) 7(3) *Journal of Environmental Policy and Planning* 185, 186-193.

<sup>42</sup> David H Cole, above n 35, 396-404.

<sup>43</sup> Ibid, 397.

<sup>44</sup> Ibid, 397.

hybrid forms in between.<sup>45</sup> Cole envisions a continuum where governance institutions and organisations are both independent of, and interdependent on, each other.<sup>46</sup> Governance based on such a continuum becomes a polycentric approach where multiple public and private organisations have a role in policy development and a joint effect on the benefits and costs of implementing such policy.<sup>47</sup> This essay argues that directors' duties are an ideal legal tool to achieve this. By engaging and empowering company directors, corporations can begin to play a meaningful role in a polycentric, bottom up approach to effectively mitigating climate change.

Support for a polycentric approach is enjoying increasing support in the academy,<sup>48</sup> and the commercial area as well. A recent report by Booz and Company argues for nationally based climate strategies that are tailored to each country's specific needs and assets.<sup>49</sup> Other investments groups have also recognised the importance of corporations taking responsibility for the impact climate change will have on their market value and taking steps to mitigate this.<sup>50</sup>

Finally, in arguing the case for a polycentric approach to climate change policy, Cole and Ostrom both insist it is capable of providing the best opportunity for experimentation, choice and learning.<sup>51</sup> It is this feature of this approach that makes it ideal for tackling the wicked nature of climate change as it brings flexibility and

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<sup>45</sup> Jouni Paavola, 'Climate Change: The Ultimate Tragedy of the Commons?' in David Cole and Elinor Ostrom (eds), *Property in Land and Other Resources* (Lincoln Institute of Land Policy, 2011) 417, 421-425.

<sup>46</sup> Cole, above n 35, 396.

<sup>47</sup> Ostrom, above n 41, 358.

<sup>48</sup> See especially Gwyn Prins et al, above n 1; Gwyn Prins and Steve Rayner, above n 1.

<sup>49</sup> 'Bottom Up and Country Led: A New Framework for Climate Change Action' (Report, Booz & Company, 2010) <[http://booz.com/global/home/what\\_we\\_think/reports\\_and\\_white\\_papers/ic-display/48841378](http://booz.com/global/home/what_we_think/reports_and_white_papers/ic-display/48841378)>.

<sup>50</sup> Ibid; KPMG Australia, *Carbon Disclosure Project Report 2006: Australia and New Zealand* (Research Report for the Investor Group on Climate Change and JBWere Goldman Sachs, 2006) <[http://www.cdproject.net/download.asp?file=CDP4\\_Australia\\_Report.pdf](http://www.cdproject.net/download.asp?file=CDP4_Australia_Report.pdf)>.

<sup>51</sup> Cole, above n 35, 406; Ostrom, above n 35, 31; Ostrom, above n 41, 359.

the ability to quickly respond to change. For corporations, this is essential if they are to be a part of the solution.

### B *The Rise of Non-state Actors*

Alongside the growing body of research criticising the top down climate change regime and advocating a more inclusive, bottom up approach is an equally burgeoning body of work examining a generalised weakening of the nation state as an entity with any real political clout. This literature shows how non-state actors such as corporations, NGOs and activist groups are increasingly involved in authoritative decision making that was previously the prerogative of sovereign states.<sup>52</sup> Maarten Hajer notably speaks of an ‘institutional void’ whereby political action to address problems takes place next to or across state institutions or international treaties, not within them.<sup>53</sup> Rather than lament the demise of the nation state as a powerful entity for policy direction, Hajer urges the recognition of a new governance style capable of meeting the demands of complex and wicked problems in need of attention.<sup>54</sup> He describes this new style of policy making ‘as much a matter of citizens (and their associations) and enterprises acting in a concerted way as it is a matter of direct government intervention.’<sup>55</sup>

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<sup>52</sup> See, eg, David Vogel, ‘Private Global Business Regulation’ (2008) 11 *Annual Review of Political Science* 261, 264; Dan Danielsen, ‘How Corporations Govern: Taking Corporate Power Seriously in Transnational Regulation and Governance’ (2005) 46(2) *Harvard International Law Journal* 411, 413-416; Virginia Haufler, ‘Self-regulation and Business Norms: Political Risk, Political Activism’ in A Claire Cutler, Virginia Haufler and Tony Porter (eds), *Private Authority and International Affairs* (State University New York Press, 1999) ch 8.

<sup>53</sup> Maarten Hajer, ‘Policy without Polity? Policy Analysis and the Institutional Void’ (2003) 36(2) *Policy Sciences* 175, 175.

<sup>54</sup> *Ibid*, 189.

<sup>55</sup> *Ibid*, 191.

Corporations form part of what Kenneth Abbott and Duncan Snidal have described as the ‘governance triangle’.<sup>56</sup> This concept refers to the complex policy negotiation arrangements in place between nation states, corporations and NGOs. Although they form an important part of the governance triangle, corporations have not been included in the development and implementation of effective climate change mitigation policy. This has been to the detriment of all. The recognition of corporations’ potential to play a real and important part in the climate change solution is central to this essay. Very few commentators address the potential for corporations to play a direct role in climate change policy development, and commentary on how directors’ duties specifically could be harnessed in the process is absent entirely. Up until now, corporations have been included in the debate only to the extent that they should be responsible for paying for their GHG emissions as part of ETSs or how various corporate social responsibility initiatives might be relevant to climate change. The potential for corporations to play a key role in the climate change solution has been all but ignored by nation states, and this, it is argued, cannot continue if climate change is to be effectively addressed.

### *C The Enforceability Conundrum*

Despite the significant increase in power and influence of non-state actors over the last few decades, they do not, and should not, hold the place of law makers. An obvious argument against a more inclusive, bottom up approach to policy making is that corporations and other non-state actors lack authority to implement and enforce anything. There is a view that sovereign states are the most appropriate bodies to be making decisions around climate change mitigation as only these actors can put in

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<sup>56</sup> See Kenneth Abbott and Duncan Snidal, ‘The Governance Triangle: Regulatory Standards Institutions and the Shadow of the State’ (Working Paper, Global Governance Project, Oxford University, 2006); Kenneth Abbott, ‘Engaging the Public and the Private in Global Sustainability Governance’ (2012) 88(3) *International Affairs* 543, 546-549.

place legitimately enforceable regulation.<sup>57</sup> It is not denied that most of the ‘regulation’ peddled by non-state actors such as activist groups and the compilers of industry practice guidelines come in the form of voluntary codes and standards which, by definition, lack the legitimacy and enforcement mechanisms of hard law.<sup>58</sup>

In addition, many commentators rightly remain sceptical of efforts by profit-seeking firms to develop and adopt practices that are grounded in morality, as climate change mitigation efforts can be seen to be.<sup>59</sup> For this reason, this essay argues that the inclusion of corporations at the climate change policy negotiation table must, first, be accompanied by legal enforcement, and, second, focus on the economic benefits for corporations. An often forgotten dimension of climate change is its impact on business; the focus is more often than not on the impact of corporate activity on the climate. Corporations are responsible for almost all significant environmental impacts, be it through the use of natural resources, waste production, GHG emissions and water and energy use.<sup>60</sup> They are also among the largest emitters of GHG which is directly responsible for global warming.<sup>61</sup> The environment, in turn, has a huge impact on business through events such as natural disasters, drought, legal restrictions protecting threatened species and heritage listings and, of course, climate change.<sup>62</sup> Directors’ duties have been identified as ideal legal tools for the job

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<sup>57</sup> David Vogel, above n 52, 264.

<sup>58</sup> Ibid; Ronnie D Lipschutz and Cathleen Fogel, ‘Regulation for the Rest of Us? Global Civil Society and the Privatisation of Transnational Regulation’ in Rodney Bruce Hall and Thomas J Biersteker (eds), *The Emergence of Private Authority in Global Governance* (Cambridge University Press, 2002) ch 6, 115; Virginia Haufler, ‘Global Governance in the Private Sector’ in Christopher May (ed), *Global Corporate Power* (Lynne Rienner, 2006) ch 5, 85.

<sup>59</sup> The ethical foundations of climate change are not addressed in this essay. For an overview of some of the ethical dimensions of the climate change debate, see, eg, Rosemary Lyster, above n 20; Mark Stallworthy, above n 20; Rowena Maguire and Bridget Lewis, above n 20; Jeremy Baskin, above n 20; Sujatha Byravan and Sudhir Chella Rajan, above n 20; Achala Chandani, above n 20.

<sup>60</sup> Karen Bubna-Litic, ‘Climate Change and Corporate Social Responsibility: The Intersection of Corporate and Environmental Law’ (2007) 24 *Environmental and Planning Law Journal* 253; Douglas G Cogan, ‘Corporate Governance and Climate Change: Making the Connection’ Investor Responsibility Research Centre Report (Ceres, 2006).

<sup>61</sup> Douglas G Cogan, above n 60.

<sup>62</sup> Ibid.



because not only do they come with established enforcement mechanisms, but they are also geared to focus sharply on corporate success.

#### IV THE ROLE OF CORPORATIONS IN A BOTTOM UP APPROACH

At its heart, this essay's argument is not about harnessing a bottom up, polycentric approach to tackling wicked problems. Nor is it about the very best way to manage climate change, or ensuring future generations have equal access to the Earth's natural resources. It's about recognising that corporations are, at *their* heart, constructs of community values, and that they derive their legitimacy and privilege only through continuing to behave in a way that is consistent with those values. Equally importantly, it is also about the recognition that these community values can and do change, and that corporate behaviour is expected to change correspondingly. It is by abiding by these values and exhibiting acceptable standards of behaviour that corporations obtain their real 'licence to operate'<sup>63</sup> – incorporation is but the first step in an ongoing procedure to maintain legitimacy.

To know this to be true, one only has to look at the worldwide community revolt and condemnation that occurs when the most egregious of corporate behaviour is exposed, as, for example, in the cases of Enron<sup>64</sup> and James Hardie.<sup>65</sup> These examples of forceful community reaction to instances of corporations not behaving as they are expected to show that corporations do not exist in isolation. Corporations are undeniably intricately involved in the lives of members of the community and an important part of modern society. Thus, when modern society faces a problem as serious as climate change, and it can be said that corporations both played a large

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<sup>63</sup> R Edward Freeman, above n 5, 31; Neil Gunningham, Robert A Kagan, Dorothy Thornton, 'Social License and Environmental Protection: Why Businesses Go Beyond Compliance; (2006) 28(2) *Law and Social Inquiry* 307; Neil Gunningham, Dorothy Thornton and Robert A Kagan, 'Motivating Management: Corporate Compliance in Environmental Protection' (2005) 27(2) *Law and Policy* 289.

<sup>64</sup> William W Bratton, 'Enron and the Dark Side of Shareholder Value' (2002) 76 *Tulane Law Review* 1275.

<sup>65</sup> See generally Edwina Dunn, 'James Hardie: No Soul to be Damned and No Body to Be Kicked' (2005) 27 *Sydney Law Review* 339; Lee Moerman and Sandra van der Laan, 'Pursuing Shareholder Value: The Rhetoric of James Hardie' (2007) 31(4) *Accounting Forum* 354.

role in causing that problem and hold the potential to play a significant role in managing it, is it not logical that the community would alter the terms of its licence to operate to require corporations to do what they can to be a part of the solution? Directors' duties are a primary means by which society sets the acceptable standard of corporate behaviour and they are thus an appropriate tool to engage corporations in a bottom up, polycentric approach to effective climate change mitigation.

### *A History of the Corporate Form*

Any examination of how corporate law can be utilised to mitigate climate change inevitably becomes a question of the degree to which the community believes corporations should play a role in rectifying social and environmental problems. More precisely, it becomes a question of what the community believes the proper role of corporations should be, and the matters it believes directors should concern themselves with. This question is not new; debate around the purpose of the corporation and how to delimit the wider impact of corporate activity is as old as the limited liability corporation itself. There have always been questions of the responsibilities that should accompany the rights and privileges that incorporation brings. To examine the arguments for and against directors' duties becoming a tool in an approach to climate change mitigation, we must begin with a discussion of the separate entity doctrine as it was from this doctrine that the duties grew.

#### *1 The Doctrine of Separate Entity*

The legal concept of a company as a fictitious legal person quite distinct from its managers, investors and creditors is very old.<sup>66</sup> Corporations were legal structures born of commercial need. Starting out as little more than clans and guilds, by the 16<sup>th</sup>

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<sup>66</sup> Samuel Williston 'History of the Law of Business Corporations Before 1800' (1888) 2(3) *Harvard Law Review* 105, 106.

century they had developed into the organised entities that allowed exploration of the New World.<sup>67</sup> It was this intrepid spirit that necessitated the development of the modern corporation: Building and fitting out ships for voyages typically took several years and the cost was almost always too great for any single merchant to bear. In 1600 Queen Elizabeth herself famously chartered the Company of Merchants of London to facilitate trading to the East Indies.<sup>68</sup> In its charter application, ‘one of the claims to favourable consideration... was that noblemen, gentlemen, shopkeepers, widows, orphans and all other subjects may be traders, and employ their capital in a joint stock.’<sup>69</sup> In other words, the notions of companies having several owners and those owners being separate from management were acknowledged as beneficial for two distinct reasons. Firstly, they permitted the undertaking of large scale projects that would otherwise be impossible, and secondly, they facilitated the participation of those who would otherwise be excluded. Today, this view is articulated in language of advantage and efficiency: ‘Shareholders can participate in the gains from entrepreneurial ventures even though they lack management skills, [and] managers can pursue profitable business opportunities even though they lack large personal wealth.’<sup>70</sup>

By the early 1700s, England was enjoying great economic growth, however businessmen were still constrained by a reluctance to risk their capital on new ventures as there was no protection from personal liability if the venture failed. Contract terms were inadequate to completely limit personal liability, especially for

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<sup>67</sup> Ibid, 109.

<sup>68</sup> David Macpherson, *The History of European Commerce with India* (Longman, Hurst, Orme and Brown, 1812).

<sup>69</sup> Samuel Williston, above n 66, 109.

<sup>70</sup> Daniel R Fischel, ‘The Corporate Governance Movement’ (1982) 35(6) *Vanderbilt Law Review* 1259, 1262.

unanticipated loss.<sup>71</sup> While incorporation had brought the benefits of exploration to wider society, businessmen were still exposed to significant risk. Eventually, the decision in *Salomon v Salomon & Co Ltd*<sup>72</sup> definitively established that a company is separate from its owners such that the company owns assets and can accrue benefits and liabilities. In its decision, the House of Lords, unlike the lower courts, read the then Companies Act as conveying legislative intent. The lower courts had taken the view that reading the legislation ‘ahistorically, would distort the well-known intentions of the Act’s drafters’ and that this would go against the expectations of the commercial world.<sup>73</sup>

The House of Lords’ decision shows that even at this nascent stage of the doctrine’s development, Parliament was given ultimate responsibility for changing the doctrine when it no longer met changing social or commercial needs. Not long after this decision, the same view was affirmed in Australia with the court finding that ‘when a company acts it does so in its own right and not just as an alias for its controllers.’<sup>74</sup> Since then, the doctrine of separate entity ‘has continued unexpurgated from Anglo-Australian corporate law.’<sup>75</sup> Even this brief history of the corporate form illustrates clearly how corporate law has generally developed in response to changing commercial, economic and social needs. This essay argues that climate change has brought about a change in what the community needs from corporations, and that corporate law is now due for another corresponding change.

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<sup>71</sup> Robert Austin and Ian Ramsay, *Fords Principles of Corporations Law* (14<sup>th</sup> ed, 2010) 6.

<sup>72</sup> [1897] AC 22.

<sup>73</sup> Roman Tomasic, ‘The Modernisation of Corporations Law: Corporate Law Reform in Australia and Beyond’ (2006) 19 *Australian Journal of Corporate Law* 2, 12-13.

<sup>74</sup> *Gas Lighting Improvement Co Ltd v Inland Revenue Commissioners* (1923) AC 723, per Lord Sumner, 740-741.

<sup>75</sup> Ian M Ramsay and David B Noakes, ‘Piercing the Corporate Veil in Australia’ (2001) 19 *Company and Securities Law Journal* 250, 252.

## *2 What is the Purpose of a Corporation?*

Since the 17<sup>th</sup> century, it has been accepted that the object of a business is twofold: the public one of managing and ordering the trade in which the business is engaged, as well as the private one of profit for its members.<sup>76</sup> However, there has never been a shortage of commentators who believe corporations owe a social obligation. The 1919 American case of *Dodge v Ford*<sup>77</sup> aimed to settle the issue when it held that ‘a business organisation is organised and carried on primarily for the profit of the stockholders.’ Debate has nevertheless continued apace. The famous debate between Adolf Berle and Merrick Dodd<sup>78</sup> in the early 1930s brought the tension between competing beliefs about corporate responsibility into the academic arena. Berle argued that all powers granted to a corporation and its management were ‘exercisable only for the ratable benefit of all the shareholders.’<sup>79</sup> Dodd argued that public opinion, which makes law, was on the side of businesses having ‘a social service as well as a profit-making function...’<sup>80</sup> In his famed opinion piece in the *New York Times Magazine* in 1970, Milton Friedman declared any corporate activity outside of the narrow purpose of achieving shareholder desires to be ‘unadulterated socialism’ and claimed it impossible for a business, as a fictional legal construct, to have social responsibility.<sup>81</sup> Like Berle, Friedman believed that corporations in a free enterprise, private property system should aim solely to increase the wealth of their shareholders.

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<sup>76</sup> Samuel Williston, above n 66, 111.

<sup>77</sup> *Dodge Brothers v Ford Motor Company*, 170 NW 668, (Mich. 1919).

<sup>78</sup> E Merrick Dodd, ‘For Whom are Corporate Managers Trustees?’ (1931) 45 *Harvard Law Review* 1145; Adolf A Berle, ‘Corporate Powers as Powers in Trust’ (1930) 44 *Harvard Law Review* 1049.

<sup>79</sup> Adolf A Berle, above n 78, 1049.

<sup>80</sup> E Merrick Dodd, above n 78, 1148.

<sup>81</sup> Milton Friedman, ‘The Social Responsibility of Business is to Increase its Profits’ (13 September 1970) *The New York Times Magazine*.

In the 1970s and 1980s when ideas such as corporate social responsibility and stakeholder theory first began to take hold in community consciousness, there was fierce support from academic and government circles for preservation of the status quo. Berle and Dodd's ideals were once again sparing, showing, if nothing else, that the corporation as an institution was still the focal point for much of the debate around how society operates, and who should enjoy the benefits of incorporation. The debate is still very much a live issue in Australia and much of the common law world. In 2006, the Australian Parliament held two inquiries to investigate in whose interests company directors should govern. While these inquiries concluded that no change to Australian corporate law was warranted, they nevertheless added fuel to the already fiery debate. These inquiries and their results are discussed in part VIII.

Since the *Dodge v Ford*<sup>82</sup> decision, the view in Australia at common law and under the *Corporations Act 2011* (Cth) ('*Corporations Act*') is that a director's duty to act in the best interests of the corporation requires a director to govern solely in the interests of shareholders, with the view to maximising their wealth.<sup>83</sup> In Australia and most of the common law world, this notion of shareholder primacy has persisted more or less untrammelled for nearly a century, leading irresistibly to the conclusion that the purpose of the corporate form is wealth maximisation for the shareholders. Australian legislation certainly provides no fundamental statements on the meaning and purpose of a company or its responsibilities which suggest otherwise.<sup>84</sup> Given

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<sup>82</sup> *Dodge Brothers v Ford Motor Company*, 170 NW 668, (Mich. 1919).

<sup>83</sup> Mark Standen, 'The Corporation in Society: Time to Revise its Role?' (2006) 87 *Reform Issue* 13.

<sup>84</sup> Although 'company' is defined in s 9 of the *Corporations Act 2001* (Cth), as a company registered under the Act, it is not a particularly satisfying definition as it does not tell us what a company is, as it can include registerable bodies such as unincorporated associations. Section 57A also defines corporation, which includes a company, a body corporate and an unincorporated body. As a result, there is little guidance or direction on fundamentally what a company is supposed to be.

that corporate law in Australia has undergone significant change in recent decades<sup>85</sup> and that Parliament can at any time elect to make changes to the law, legislative silence on the issue of the status of non-shareholder stakeholders supports a sturdy theoretical argument that using corporate resources for anything other than the benefit of shareholders (such as social or charitable causes) is ‘neither permissible nor prudent.’<sup>86</sup>

This debate is important to this essay as directors’ duties are essentially mandates to uphold the community’s view of who the corporation should serve. The thesis of this essay is that directors must be allowed to aggressively pursue the interests of shareholders or the economic benefits of incorporation will be lost, however, this pursuit must be tempered by the need to balance the interests of other important stakeholders, specifically the climate and future generations. This will require the reconciliation of two theories of firm organisation – the economic theory of firms, and stakeholder theory.

### B *The Economic Theory of Firms*

Limited liability, the doctrine of separate entity and the goal of securing maximum benefit for shareholders have together come to be known as the economic theory of firms. This theory states that managers require a criterion for evaluating firm performance and that it should be maximisation of the long-term market value of the firm.<sup>87</sup> As market value translates directly to shareholder value, the shareholder primacy model is enshrined by the economic theory of firms. Frank Easterbrook and

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<sup>85</sup> For example, the *Corporations Act 2001* (Cth) was the result of the enactment of referral legislation by the Australian States. The *Corporations Act 2001* replaced the *Corporations Act 1989* (Cth) as well as the eight *Corporations Laws* of the States and Territories.

<sup>86</sup> Milton Friedman, above n 81.

<sup>87</sup> Michael C Jensen, ‘Value Maximisation, Stakeholder Theory and the Corporate Objective Function’ (2001) 14(3) *Journal of Applied Corporate Finance* 8, 9.



Daniel Fischel, two eminent scholars in this area, argue unequivocally that corporations should not concern themselves with social issues and that any attempt to do so amounts to theft from shareholders.<sup>88</sup> As shown by the discussion above, this theory has been a foundation principle of modern Australian corporate law. Consequently, the *Corporations Act* may be viewed as a code for shareholder rights: Share price and dividend payments are primary indicators of corporate health and capital and share markets are the key sites of corporate activity.

The economic theory of firms is countered by the growing body of management literature that puts forward stakeholder theory. This approach, discussed in part V, acknowledges that corporations depend on many stakeholders other than shareholders for their survival. The theory encourages managers to go beyond their minimum legal commitments in accommodating non-shareholder stakeholders with the aim of ensuring corporate survival. This essay argues for a legal environment which brings together features of both theories to achieve two things. First, corporate law should permit corporations to pursue their goals and achieve large, even extraordinary, profits. It should encourage management decisions that ensure investors can enjoy a return. Second, this legal environment should impose a duty on directors to take into account the interests of the climate and future generations.

It is acknowledged that these statements contain several degrees of vagueness: fairness, futurity and even what might constitute a large profit are all nebulous concepts. In response to this point it is argued that corporate law, as a legal tool, is ideally equipped to deal with the fickle vagaries of human nature, and the sometimes conflicting desires of company owners and the community. That is what it is

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<sup>88</sup> Frank H Easterbrook and Daniel R Fischel, *The Economic Structure of Corporate Law* (Harvard University Press, 1991), 1-39.

designed to do. The principles of stakeholder theory and intergenerational equity are called upon to inform this new duty. These principles are discussed in parts V and VI.

It is worth noting here that a views as narrow as Friedman's, Easterbrook's and Fischel's would struggle to find ardent supporters among company directors and shareholders today. These groups now generally recognise and accept that businesses do incur moral obligations by virtue of being allowed access to the benefits of incorporation.<sup>89</sup> The growth in the 'ethical investment' sector is testament to this. According to Ethical Investment Research Services, the total value of assets under ethical investment was approximately €7.6 trillion in September 2010, with approximately €58 billion in Australia and New Zealand alone.<sup>90</sup>

### *C What About Non-shareholder Stakeholders Affected by Corporate Activity?*

#### *Conflicting Laws and Values?*

Michael Jensen uses the question 'How does the community want the corporations in its economy to measure their performance?' as a way to identify the values important to the community at any given time.<sup>91</sup> He compares the economic theory of the firm, which supports shareholder wealth maximisation, with stakeholder theory which seeks to ensure that a broader group of parties on whom the corporation relies for survival have their interests taken into account by company management.

Stakeholder theory is discussed in detail in part V. Central to Jensen's argument is the notion that while stakeholder theory has its place, it is incomplete as it is unable

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<sup>89</sup> While Milton Friedman certainly acknowledged the requirement for directors to act in accordance with 'ethical custom' this was but a cursory nod to avoiding egregious breaches of decency. See Milton Friedman, above n 81.

<sup>90</sup> Ethical Investment Research Services, 'State of Responsible Business (Asia)' (Report, September 2011) <<http://www.eiris.org/files/research%20publications/EIRISResponsibleBusinessASIA2011.pdf>>.

<sup>91</sup> Michael C Jensen, above n 87, 8.

to 'keep score' – that is, it provides no yardstick with which to measure corporate performance. He argues that the maximisation of the long-run value of the firm should be the criterion for trade-term decisions between stakeholders and that only the economic theory of firms can provide this.<sup>92</sup> He contends that stakeholder theory permits an inappropriate diversion of corporate resources away from shareholders and allows for opportunistic managers to act in their own self-interest by claiming an action benefits a stakeholder group.<sup>93</sup>

Of course, a director's duty to act in the best interests of the corporation and its shareholders does not require the director to act at the expense of the interests of other stakeholders. Indeed, it will often be in the interests of the corporation that appropriate recognition is given to the interests of other groups including employees, customers, contractors, the community and the environment. The existing law recognises this and 'already provides a significant degree of flexibility which facilitates due consideration of the interests of such stakeholders...'<sup>94</sup> This flexibility does go some way to preserving the balance between shareholders' and other stakeholders' interests, although only as far as a being part of a broader consideration of what is in the interests of the corporation as a whole.<sup>95</sup>

The example of corporate philanthropy is apt. It is now common practice for corporations to donate money to charitable causes. There is research to suggest that such actions work in the company's favour because of the reputational benefits that flow from them.<sup>96</sup> Former Chief Justice of the High Court, Sir Brennan, notes

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<sup>92</sup> Ibid.

<sup>93</sup> Michael C Jensen, above n 87; Alexei M Marcoux, 'Balancing Act' in Joseph R Des Jardins and John J McCall (eds), *Contemporary Issues in Business* (Wadsworth, 4th ed, 2000) 92.

<sup>94</sup> Mark Standen, above n 83, 13.

<sup>95</sup> Ibid, 13.

<sup>96</sup> Karina Funk, 'Sustainability and Performance' [2003] (Winter) *MIT Sloan Management Review* 65.

however, that modern commentators and corporate practice suggest that it is permissible to donate corporate assets only if the donation is likely to result in a benefit for the corporation, and that donations without the prospect of benefit are not authorised.<sup>97</sup> Sir Brennan cited Lord Justice Bowen's judgment in *Hutton v West Cork Railway*<sup>98</sup> as the doctrine governing the application of a corporation's assets. Lord Justice Bowen said managers

...can only spend money which is not theirs but the company's if they are spending it for the purposes which are reasonably incidental to the carrying on of the business of the company... The test must be what is reasonably incidental to, and within the reasonable scope of carrying on, the business of the company.<sup>99</sup>

Despite this, companies are increasingly asked to provide 'innovative solutions to deep-seated problems of human misery.'<sup>100</sup> Former UN Secretary-General, Kofi Annan even claimed that 'by joining the global fight against HIV/AIDS, ...business will see benefits on its bottom line.'<sup>101</sup> This belief that corporations should play a part in alleviating social problems is directly at odds with the economic theory of the firm, and the duty to act in the interests of shareholders. Attracting frequent commentary by high profile figures and parliamentary attention in the form of inquiries demonstrates that that this is a live issue and suggests that corporate law is due for reform to rebalance the interests of stakeholders and redefine directors' responsibilities.

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<sup>97</sup> Sir Gerard Brennan, 'Law, Values and Charity' (2002) 76 *The Australian Law Journal* 492.

<sup>98</sup> *Hutton v West Cork Railway Co* (1883) 23 Ch D 654, 671 per Bowen LJ.

<sup>99</sup> *Ibid.*

<sup>100</sup> Joshua D Margolis and James P Walsh, 'Misery Loves Companies: Rethinking Social Initiatives by Business' (2003) 48(2) *Administrative Science Quarterly* 268, 268.

<sup>101</sup> Kofi Annan, 'Unparalleled Nightmare of AIDS' (Speech delivered at the United States Chamber of Commerce, Washington, DC, 2001) <<http://www.un.org/News/Press/docs/2001/sgsm7827.doc.htm>>.

### *D Corporations and Corporate Law as Social Constructs*

The history of the corporate form and the rigorous debate around the purpose of the corporation, both outlined above, clearly show that corporations are not spontaneous creations but the result of the adaptation of earlier institutions in response to changing commercial and social need. Parliament's decision to grant corporations the benefits of limited liability and the doctrine of separate entity is vindicated on economic grounds.<sup>102</sup> It is important to remember that Parliament does not, however, grant an 'unfettered freedom to incorporators and their companies.'<sup>103</sup> As William Bratton eloquently puts it,

[t]he state clearly reserves the right to rewrite the ground rules and to constrain the freedom of corporate actors. Even as corporate law lets the participants proceed, it in effect cautions them that they may act at will only if on good behaviour. Corporate law facilitates private behaviour, but with a reservoir of suspicion and a threat of constraint.<sup>104</sup>

The corporate form's ability to continuously adapt to a changing environment shows it is a remarkably resilient legal institution. It has survived hundreds of years of industrialisation, modernisation and law reform.<sup>105</sup> The doctrine of separate entity, as a cornerstone of corporate law, has also developed in response to changing commercial needs. Today it reflects a desire for a laissez-faire market providing

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<sup>102</sup> Michael Whincop, 'Overcoming Corporate Law: Instrumentalism, Pragmatism and the Separate Legal Entity Concept' (1997) 15 *Company and Securities Law Journal* 411, 471.

<sup>103</sup> John A Purcell and Janice A Loftus, 'Corporate Social Responsibility: Expanding Directors' Duties or Enhancing Corporate Disclosure' (2007) 21 *Australian Journal of Corporate Law* 135.

<sup>104</sup> William Bratton, 'The 'Nexus of Contracts' Corporations: A Critical Appraisal' (1988-1989) 74(407) *Cornell Law Review* 445, 445.

<sup>105</sup> Katharina Pistor, Yoram Keinan, Jan Kleinheisterkamp and Mark D West, 'The Evolution of Corporate Law: A Cross-Country Comparison' (2002) 23 *University of Pennsylvania Journal of International Economic Law* 791, 793-794.

perfect freedom for investors and entrepreneurs.<sup>106</sup> However, this separation of management and ownership brought its own set of risks. It was recognised early on that directors were in a position to use investor funds for their own advantage, and, because of limited liability, escape liability. Directors' duties were introduced to protect investors and uphold the values of trust and integrity in the commercial arena. Wider society benefited too, as stricter controls on directors usually meant companies were better managed and less likely to fail which in turn protected employees, creditors and suppliers and upheld the values of fairness, security and economic opportunity. In this way it can be seen that directors' duties are primarily a tool for protecting society from unfair or dishonest action by those in a position of power. These duties and the risks they intend to mitigate are discussed in part VII.

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<sup>106</sup> Angelo Capuano, 'The Realist's Guide to Piercing the Corporate Veil: Lessons from Hong Kong and Singapore' (2009) 23 *Australian Journal of Corporate Law* 56, 56.

## V AN INTRODUCTION TO STAKEHOLDER THEORY

In 1984, R Edward Freeman published his landmark book, *Strategic Management: A Stakeholder Approach*,<sup>107</sup> a work that established what is now known as stakeholder theory. Since then, the literature on stakeholder theory has developed into a vast and diverse body that has had real impact on business practice. Stakeholder theory acknowledges that companies rely on the support of several different groups for their survival, and that shareholders are only part of the picture. Critically, stakeholder theory recognises that these other, non-shareholder groups can at any time withdraw their support for the corporation and that this would be disastrous for its ongoing survival. The theory examines the way corporations can interact with and manage these parties so as to shore up their support.

Although stakeholder theory first came to prominence in the 1980s and 1990s, many of its underlying principles had been discussed and debated for decades. Once again, we can turn to the voice of Dodd for a succinct and incisive summary. He said,

[i]f the unity of the corporate body is real, then there is reality and not simply legal fiction in the proposition that the managers of the unit are fiduciaries for it, and not merely for its individual members, that they are... trustees for an institution [comprised of many constituents] rather than attorneys for the stockholders.<sup>108</sup>

Freeman originally defined a stakeholder as anyone who can affect or is affected by corporate activity.<sup>109</sup> Although this definition is extremely wide, research most often identifies groups such as employees, creditors, suppliers and the community as

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<sup>107</sup> R Edward Freeman, above n 5.

<sup>108</sup> E Merrick Dodd, above n 78, 1160.

<sup>109</sup> R Edward Freeman, above n 5.

stakeholders. More recently, abstract concepts such as the environment<sup>110</sup> and future generations<sup>111</sup> have also been identified as stakeholders. Because of the rising profile of environmental issues and the intensity of debate around climate change management, stakeholder theory has enjoyed increased interest in the context of environmental policy. As a result, there is a significant body of research dedicated to the natural environment as a stakeholder.<sup>112</sup> Although this literature focuses primarily on traditional environmental issues, rather than the nuanced problems climate change presents to corporations, it nevertheless offers useful insights.

Freeman and others have recently redescribed stakeholder theory as simply ‘a theory of organizational management and ethics.’<sup>113</sup> The theory is not simplistic though; its aim is to future-proof the corporation via an approach to stakeholder management that exceeds whatever minimum obligations may be in place. Stakeholder theory is not about merely raising the profile of non-shareholder stakeholders or about pleasing more people; it argues that the benefit of being an ongoing concern can be gained by going over and above the minimum legal obligations owed by corporations to stakeholders.<sup>114</sup>

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<sup>110</sup> See, eg. Nardia Haigh and Andrew Griffiths, ‘The Natural Environment as a Primary Stakeholder: The Case for Climate Change’ (2009) 18 *Business Strategy and the Environment* 347; Mark Starik, ‘Should Trees Have Managerial Standing? Towards Stakeholder Status for Non-Human Nature’ (1995) 14 *Journal of Business Ethics* 207.

<sup>111</sup> Auditor General Victoria, ‘Beyond the Triple Bottom Line: Measuring and Reporting on Sustainability’ (Occasional Paper, Victorian Auditor-General’s Office, June 2004) <<http://www.audit.vic.gov.au/publications/2004/20040615-Reporting-Measuring-Sustainability.pdf>>; Kevin Barnes and Beverley Lord, ‘Intergenerational Equity: Treatment of Infrastructure in Local Government Financial Planning’ (Paper submitted to the 1<sup>st</sup> International Conference on Sustainable Management of Public and Not For Profit Organisations, Forli, Italy, 1-3 July 2009) <[http://sydney.edu.au/business/\\_data/assets/pdf\\_file/0004/56605/Intergenerational\\_Equity.pdf](http://sydney.edu.au/business/_data/assets/pdf_file/0004/56605/Intergenerational_Equity.pdf)>.

<sup>112</sup> See, esp. Jean Stead and Ed Stead, *Management for a Small Planet: Strategic Decision Making and the Environment* (Sage, 1992).

<sup>113</sup> Robert Phillips, R Edward Freeman and Andrew C Wicks, ‘What Stakeholder Theory is Not’ (2003) 13(4) *Business Ethics Quarterly* 479, 480.

<sup>114</sup> R Edward Freeman, above n 5; R Edward Freeman, Jeffrey S Harrison and Andrew C Wicks, *Managing for Stakeholders: Survival, Reputation and Success* (Yale University Press, 2007).



### *A Stakeholder Theory and the Purpose of the Corporate Form*

Once again, questions of the purpose of the corporation become relevant. Stakeholder theory acknowledges that companies rely on the support of several different groups for their existence, and that shareholders do not provide all the support necessary for corporate survival. Because of this, corporations must behave in a manner that ensures the continued support of non-shareholder stakeholders. Usually, this will involve the expenditure of resources. For this reason stakeholder theory can be controversial because some consider it as a departure from the long-dominant economic theory of firms.<sup>115</sup> Critics of stakeholder theory argue that it is an excuse for managerial opportunism,<sup>116</sup> and that, unlike the economic theory of firms, it cannot provide the necessary measurement criteria and specific objective functions for the corporation.<sup>117</sup> The founders of stakeholder theory say this is something of a misinterpretation, and that the theory's true goal is continued survival of the organisation, not to provide a performance measurement tool.<sup>118</sup>

This essay argues that that stakeholder theory can inform a 'clumsy' solution to the wicked problem of climate change. Not only does it provide an established theoretical framework for dealing with multiple demands on corporate resources, but it also avoids the problems introduced by a top down approach to climate change mitigation by pushing decision making power down to the level of company directors. This approach does not unreasonably compromise shareholder primacy and the benefits brought by that model. Rather, it empowers company directors to take

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<sup>115</sup> R Edward Freeman et al, *Stakeholder Theory: The State of the Art* (Cambridge University Press, 2010) 4-5 10-12.

<sup>116</sup> Michael C Jensen, 'Value Maximisation and the Corporate Objective Function' in Michael Beer and Nitin Nohria, *Breaking the Code of Change* (Harvard Business School Press, 2000) 37; Alexei M Marcoux, above n 93; Elaine Sternberg, *The Stakeholder Concept: A Mistaken Doctrine* (Foundation for Business Responsibilities, 2001).

<sup>117</sup> Michael C Jensen, above n 87, 9.

<sup>118</sup> R Edward Freeman, Jeffrey S Harrison and Andrew C Wicks, above n 114, 481.

into account the interests of future generations and the global climate in a manner that better ensures firm survival. Importantly, this approach does not straitjacket management strategy, but permits creativity and innovation in decision making by advocating for a balancing of the needs of these three important stakeholders: shareholders, the climate and future generations.

### *B Stakeholder Theory: Informing a Bottom Up Approach to a Wicked Problem*

Stakeholder theory was first developed in response to the problems brought about by a rapidly changing business environment. It sought to explain how business survival could be understood in a modern arena which was experiencing change at a rate not seen before.<sup>119</sup> There are three main problems the theory aims to address. These are problems of value creation and trade in different national, industrial and societal contexts; ethical problems brought about by capitalism and globalisation and a managerial mindset that can makes it difficult to combine economic theory and business ethics when making decisions.<sup>120</sup> The problem of climate change could be said to embody all three of these problems – it has created great turbulence in the business arena, it spans all nations, industries and societies, it has the potential to strike at the heart of capitalism, it is certainly a global problem and, although they are not discussed in detail in this essay, it is a problem with significant justice and ethical dimensions.<sup>121</sup> Because of the way climate change presents the very problems stakeholder theory sets out to address, and because of the way it interacts directly with corporate activity, it is argued that climate change could be effectively mitigated by a bottom up approach that incorporates principles of stakeholder theory.

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<sup>119</sup> R Edward Freeman et al, above n 115, 4.

<sup>120</sup> Ibid, 4-6.

<sup>121</sup> For a more detailed discussion of the ethical components of climate change, see, eg, Rosemary Lyster, above n 20; Mark Stallworthy, above n 20; Rowena Maguire and Bridget Lewis, above n 20; Jeremy Baskin, above n 20; Sujatha Byravan and Sudhir Chella Rajan, above n 20; Achala Chandani, above n 20.

Thanakvaro De Lopez examines the application of stakeholder theory in an environmental conservation context and identifies a number of challenges facing the theory in this arena. Chief among these are that there will always be situations where there will be trade-offs between the environment and development, and that the management of stakeholders takes the form of seeing that the objectives of primary stakeholders are achieved and that other stakeholders are satisfied where it is possible to do so.<sup>122</sup> Although these issues were investigated in a traditional environmental context, they can also be applied to stakeholder theory in a climate change context. This essay proposes that in a climate change context it is shareholders, the climate itself and future generations who should be considered primary stakeholders. It is the interests of these three groups that should be considered first, with all other stakeholders being satisfied where possible.

While placing these three stakeholders as equal firsts may appear as an attempt to avoid some of the difficult questions around whose interests take priority, De Lopez's first point assists here. That is that trade-offs are inevitable, and that in the model proposed here, trade-offs will occur between these primary stakeholders. It is argued that as sophisticated and informed decision makers, who are already accustomed to balancing conflicting needs, company directors are well equipped to deal with managing these trade-offs in a way that minimises harm and ensures as much fairness as possible. Because climate change is as much a problem of economics and production as it is of changing climate, these trade-offs mean that sometimes shareholders' interests will come second to those of the climate and future generations, and sometimes vice versa.

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<sup>122</sup> Thanakvaro De Lopez, 'Stakeholder Management for Conservation Projects: A Case Study of Ream National Park, Cambodia' (2001) 28(1) *Environmental Management* 47, 52-55.

## C Stakeholder Taxonomy

One of the primary criticisms of stakeholder theory is that it could allow stakeholders who do not have legitimate claims to place demands upon the organisation, affecting the interests of those who do have legitimate claims.<sup>123</sup> To counteract this problem, much of the literature has focused on different ways to distinguish, categorise and prioritise classes of stakeholders.<sup>124</sup> An important part of the stakeholder theory literature is that which investigates how company directors can identify genuine stakeholders and under what circumstances stakeholders have justifiable claims over the firm and its resources.<sup>125</sup> Proponents of stakeholder theory have developed a stakeholder taxonomy to assist managers confronted by a variety of demands from a range of stakeholders.

Stakeholder taxonomy makes distinctions between primary and secondary stakeholders,<sup>126</sup> active and passive stakeholders<sup>127</sup> and their importance and capacity to exert influence.<sup>128</sup> Although there is no unified view on how stakeholder priority

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<sup>123</sup> Ronald K Mitchell, Bradley R Agle and Donna J Wood, 'Toward a Theory of Stakeholder Identification and Salience: Defining the Principle of Who and What Really Count' (1997) 22(4) *Academy of Management Review* 853, 857; Elaine Sternberg, above n 116; Michael C Jensen, above n 87.

<sup>124</sup> Mary R English, 'Who Are the Stakeholders in Environmental Risk Decisions? How Should They Be Involved?' [2000] 11 *Risk: Health, Safety and Environment* 243, 249-250; Tiina Onkila, 'Multiple Forms of Stakeholder Interaction in Environmental Management: Business Arguments Regarding Differences in Stakeholder Relationships' (2011) 20 *Business Strategy and the Environment* 379, 384-390; David Christopher Sprengel and Timo Busch, 'Stakeholder Engagement and Environmental Strategy – The Case for Climate Change' (2010) 20 *Business Strategy and the Environment* 351, 358-360; Ronald K Mitchell, Bradley R Agle and Donna J Wood, above n 124; Jeffrey Pfeffer and Gerald R Salancik, *The External Control of Organizations: A Resource Dependency Perspective* (Harper and Row, 1978); Andrew L Friedman and Samantha Miles, 'Developing Stakeholder Theory' (2002) 39(1) *Journal of Management Studies* 1; Jeff Frooman 'Stakeholder Influence Strategies' (1999) 24(2) *Academy of Management Review* 191.

<sup>125</sup> Joshua D Margolis and James P Walsh, above n 100, 272-273.

<sup>126</sup> See, eg, Max B E Clarkson, *The Corporation and Its Stakeholders: Classic and Contemporary Reading* (University of Toronto Press, 1998).

<sup>127</sup> See, eg, Grant T Savage et al, 'Strategies for Assessing and Managing Organizational Stakeholders' (1991) 5(2) *Academy of Management Executive* 51.

<sup>128</sup> See, eg, John Kaler, 'Morality and Strategy in Stakeholder Identification' (2002) 39(1/2) *Journal of Business Ethics* 91; Robin Grimble and Kate Wellard, *Stakeholder Methodologies in Natural Resource Management: A Review of Principles, Contexts, Experiences and Opportunities* (Paper presented at the Overseas Development Administration (ODA) Natural Resources Systems Programme (NRSP) Socioeconomic Methodologies Workshop, 29–30 April, 1996, London, UK).

should be assessed, measures of power, legitimacy, urgency and proximity are useful.<sup>129</sup> Power refers to the capacity of a stakeholder to impact the firm, or threaten its survival. It also includes the ability of a stakeholder to influence others to bring about a result.<sup>130</sup> Legitimacy is a measure of the stakeholder's authority or standing in the community. It looks to standards of behaviour that make a stakeholder one that 'really counts.'<sup>131</sup> Urgency examines how immediate the stakeholder's threat appears to be and whether immediate action is required to address the stakeholder's demands.<sup>132</sup> Proximity has a spatial dimension and considers how close to the corporation a stakeholder is. For example, is it in the same community, the same network, industry or supply chain?<sup>133</sup> Shareholders are clearly stakeholders who rate highly in each of these categories. The way in which future generations and the climate qualify are discussed below.

### 1 *The Climate as a Primary Stakeholder*

Climate change has become a significant issue for business, not only because of increased community concern about the impact of corporate activity on the climate, but because of the climate's impact on business itself. The financial impact of unpredictable and increasingly frequent natural disasters is significant.<sup>134</sup> Climate change is often framed as a moral or justice issue<sup>135</sup> that corporations should address in order to meet their own ethical obligations. This leads to debate around the

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<sup>129</sup> See, eg, Cathy Driscoll and Mark Starik, 'The Primordial Stakeholder: Advancing the Conceptual Consideration of Stakeholder Status for the Natural Environment' (2004) 49(1) *Journal of Business Ethics* 55; Robert Phillips, 'Stakeholder Legitimacy' (2003) 13(1) *Business Ethics Quarterly* 25.

<sup>130</sup> Ronald K Mitchell, Bradley R Agle and Donna J Wood, above n 124.

<sup>131</sup> Ibid.

<sup>132</sup> Ibid.

<sup>133</sup> Cathy Driscoll and Mark Starik, above n 130, 130.

<sup>134</sup> Edward Mills, Eugene Lecomte and Andrew Peara, 'Insurers in the Greenhouse' (2002) 21(1) *Journal of Insurance Regulation* 4; Nicholas Stern, *The Economics of Climate Change: The Stern Review* (Cambridge University Press, 2006).

<sup>135</sup> For a discussion on how some view corporations as having a role in climate change justice see, eg, Rosemary Lyster, above n 20; Mark Stallworthy, above n 20; Rowena Maguire and Bridget Lewis, above n 20; Jeremy Baskin, above n 20; Sujatha Byravan and Sudhir Chella Rajan, above n 20; Achala Chandani, above n 20.

purpose of a corporation and difficult questions about the logic behind using the corporate form as a tool for addressing such issues. Nardia Haigh and Andrew Griffiths make a compelling argument that these ethical aspects are overshadowed by the damage climate change can do to company infrastructure, resources, products and markets.<sup>136</sup> In this way, they demonstrate how the climate ranks high on all measures of stakeholder classification and is justifiably a primary stakeholder.

## *2 Future Generations as a Primary Stakeholder*

In the case of future generations, a more nuanced examination of stakeholder classification tools is required. It could be argued that future generations lack power entirely as they have no capacity to directly impact corporations' present operation. However, what this stakeholder lacks in power it more than makes up for in the other measures of legitimacy, urgency and proximity. Hulme makes a convincing argument that the principles of intergenerational equity, discussed in detail in part VI, are widely accepted and respected by the community.<sup>137</sup> In this way future generations attain a very high legitimacy score as they are considered a stakeholder that really counts.<sup>138</sup> Similarly, future generations are inherently proximate. The newborn are only ever a few minutes away, and by virtue of this they demand urgent attention and have a legitimate claim to primary stakeholder status.

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<sup>136</sup> Nardia Haigh and Andrew Griffiths, above n 110, 352.

<sup>137</sup> Mike Hulme, above n 17, 142-177.

<sup>138</sup> Ronald K Mitchell, Bradley R Agle and Donna J Wood, above n 124.

## VI INTERGENERATIONAL AND INTRAGENERATIONAL EQUITY

### *A An Introduction to Intergenerational Equity*

Intergenerational equity is a principle that holds all generations as partners in caring for and using the Earth's resources.<sup>139</sup> The theory calls for a minimum level of equality among generations in terms of the natural and cultural resources that are inherited by each generation.<sup>140</sup> It imposes on present generations a duty to ensure that future generations have the same opportunities to care for and use the Earth as they do.<sup>141</sup> Writings in law,<sup>142</sup> philosophy<sup>143</sup> and environmental economics<sup>144</sup> have come to recognise intergenerational equity as a norm which encompasses both the moral principle that no generation has priority over another and the notion that there should be equity between generations.

The United Nation's influential *Report of the World Commission on Environment and Development: Our Common Future*, or, as it came to be known, the *Brundtland Report*, provided a definition of sustainable development that has come to be recognised as a definition for intergenerational equity. That is, 'development that meets the needs of the present without compromising the ability of future generations to meet their own needs.'<sup>145</sup> This definition has since been developed and expanded,

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<sup>139</sup> Edith Brown Weiss, above n 6.

<sup>140</sup> Ibid.

<sup>141</sup> Ibid.

<sup>142</sup> Ibid; Edith Brown Weiss, *Intergenerational Equity: A Legal Framework for Global Environmental Change* (United Nations University, 1992).

<sup>143</sup> John Rawls, *A Theory of Justice* (Harvard University Press, 1970); Miriam Kennet and Volker Heinemann 'Green Economics: Setting the Scene. Aims, Context and Philosophical Underpinning of the Distinctive New Solutions Offered by Green Economics' (2006) 1(1-2) *International Journal of Green Economics* 68.

<sup>144</sup> Christian Azar, 'Are Optimal CO2 Emissions really optimal?' (1998) 11(3-4) *Environmental and Resource Economics* 301; Christian Azar, 'Economics and Distribution in the Greenhouse' (2000) 47 *Climatic Change* 233; Cass R Sunstein and Arden Rowell, 'On Discounting Regulatory Benefits: Risk, Money and Intergenerational Equity' [2007] *The University of Chicago Law Review* 171.

<sup>145</sup> United Nations NGO Committee on Education, *Report of the World Commission on Environment and Development: Our Common Future*, A/42/427, October 1987, < <http://www.un-documents.net/wced-ocf.htm>>.

most notably by Edith Brown Weiss and Emillio Padilla. Brown Weiss argues that there exists a 'planetary trust' whereby all humans hold the Earth's natural and cultural resources for all generations of human beings.<sup>146</sup> Humans are at once beneficiaries and trustees of this planetary trust, thus they are entitled to benefit from the Earth's resources, but must also protect them so that future beneficiaries may also benefit.<sup>147</sup> Aligning with the Brundtland Report's definition, Brown Weiss developed a widely accepted<sup>148</sup> theory of intergenerational equity consisting of three principles: options, quality and access.<sup>149</sup> The first of these, options, refers to conserving the diversity of the Earth's natural resources so that future generations can use these resources to satisfy their own needs and values. Quality means ensuring the quality of the environment is comparable, on balance, between generations. Finally, access refers to non-discriminatory access among generations to the Earth and its resources.

From early on, it was recognised in the literature that climate change is an inherently intergenerational problem with potentially serious implications for equity between present and future generations.<sup>150</sup> Intergenerational problems arise because the actions of present generations impact on the economic and ecological capacity that future generations will inherit. It is the temporal dimension of climate change that brings about this type of problem because the emissions-generating activities of one generation impact future generations' ability to interact with the Earth's natural resources in terms of the options, quality and access measures. Externalities arise between generations because future generations do not participate in decisions that

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<sup>146</sup> Edith Brown Weiss, 'The Planetary Trust: Conservation and Intergenerational Equity' (1983) 11 *Ecology Law Quarterly* 495, 498.

<sup>147</sup> Ibid; Edith Brown Weiss, 'Our Rights and Obligations to Future Generations for the Environment' (1990) 84(1) *The American Journal of International Law* 198.

<sup>148</sup> James C Wood, 'Intergenerational Equity and Climate Change' (1996) 8 *The Georgetown International Environmental Law Review* 293.

<sup>149</sup> Edith Brown Weiss, above n 146, 526-532.

<sup>150</sup> Edith Brown Weiss, *In Fairness to Future Generations* (United Nations University, 1989); James C Wood, above 148, 299-300; Emilio Padilla, 'Intergenerational Equity and Sustainability' (2002) 41 *Ecological Economics* 69, 72.



will affect them. Padilla's summary of this conundrum is both insightful and incisive. He says, 'the unborn are unable to defend their interests in current decision making, nor can they participate in the political process.'<sup>151</sup>

The notion of intergenerational equity is an internationally recognised principle in environmental law and more general 'sustainability' practice.<sup>152</sup> It is well established and accepted by all levels of Australian government, notably in the 1992 *Intergovernmental Agreement on the Environment*.<sup>153</sup> The Commonwealth Government has provided legislative recognition of this principle specifically in s 3A(c) of the *Environment Protection and Biodiversity Conservation Act 1999*.<sup>154</sup> At a State level, in 2003 the Western Australian government released its *State Sustainability Strategy* which was aimed at '...meeting the needs of current and future generations through an integration of environmental protection, social advancement and economic prosperity.'<sup>155</sup> The principle also founds instruments of climate change management. For example, Art 3 of the UNFCCC provides that

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<sup>151</sup> Emilio Padilla, above n 150, 70.

<sup>152</sup> Nicolas de Sadeleer, *Environmental Principles: From Political Slogans to Legal Rules* (Oxford University Press, 2002) 91 -225; Lee Godden and Jacqueline Peel, *Environmental Law - Scientific, Policy and Regulatory Dimensions* (Oxford University Press, 2010), 239-270.

<sup>153</sup> *Intergovernmental Agreement on the Environment* (An agreement between the Commonwealth of Australia and all Australian States and Territories, 1 May 1992, Brisbane, Queensland) <<http://www.environment.gov.au/node/13008>>.

<sup>154</sup> Section 3A(c) of the *Environment Protection and Biodiversity Conservation Act 1999* (Cth) provides:

Principles of ecologically sustainable development

The following principles are principles of ecologically sustainable development:

...

- c) the principle of inter-generational equity – that the present generation should ensure that the health, diversity and productivity of the environment is maintained or enhanced for the benefit of future generations;

...

<sup>155</sup> Government of Western Australia, *Hope for the Future: The Western Australian State Sustainability Strategy* (September 2003) 24

<[http://www.dec.wa.gov.au/publications/2/doc\\_download/2638-hope-for-the-future-the-western-australian-state-sustainability-strategy.html](http://www.dec.wa.gov.au/publications/2/doc_download/2638-hope-for-the-future-the-western-australian-state-sustainability-strategy.html)>.

Parties should protect the climate system for the benefit of present and future generations of humankind.<sup>156</sup>

Although this essay does not address the many justice and ethical issues introduced by climate change, the moral dimension of climate change is impossible to ignore entirely. Notions of intergenerational equity have invited commentary by many respected and influential religious figures<sup>157</sup> including the Archbishop of Canterbury, Dr Rowan Williams, who said, ‘We are involved in a manifestly unjust situation where those who happen to be alive at the moment are draining off the resources from the vast future community who need to live in a habitable and a just world.’<sup>158</sup> Hulme convincingly demonstrates how principles of intergenerational equity are widely recognised and accepted by society.<sup>159</sup> Based on this it is not a bow too long to draw to say that making the interests of future generations a subject of a directors’ duty is both feasible and potentially effective in achieving better management of climate change.

### *B Intragenerational Equity*

An important aspect of intergenerational equity is its duality: it encompasses not only obligations to protect and preserve natural resources, but also the right of the present generation to use and enjoy them. Known as intragenerational equity, this principle is not concerned solely with the rights of those who do not yet exist, but the rights of all who inhabit this planet.<sup>160</sup> The trust analogy is apt: Not only is the current generation

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<sup>156</sup> Article 3, *Kyoto Protocol to the United Nations Framework Convention on Climate Change* (opened to signature 11 December 1997, 2303 UNTS 148, entered into force 16 February 2005).

<sup>157</sup> Mike Hulme, above n 17, 142-177.

<sup>158</sup> Rowan Williams, ‘Climate Change: A Moral Issue’ (Speech delivered to the Tyndall Centre, London, 4 May 2006) <<http://rowanwilliams.archbishopofcanterbury.org/articles.php/1759/climate-change-a-moral-issue-address-to-the-tyndall-centre>>.

<sup>159</sup> Mike Hulme, above n 17, 142-177.

<sup>160</sup> Laura Horn, ‘Climate Change Litigation Actions for Future Generations’ (2008) 25 *Environmental and Planning Law Journal* 115, 116.

trustee, but beneficiary too. Current generations are entitled to use and benefit from the natural resources the Earth has to offer. The only proviso is that benefits must be derived in a manner that ensures future generations can do the same.

This duality is one reason why directors' duties have been identified as a potentially powerful tool in a bottom up approach to effective climate change mitigation: Directors are accustomed to balancing the needs of current shareholders with a far-sighted view of the corporation's success. Shareholders seek to derive a benefit from their investment now and in the future. To this end they are entitled to expect that the company be managed in such a way that a similar benefit can be enjoyed in the future.<sup>161</sup> That is, they are entitled to expect their current as well as their future interests are being considered by company management. When viewed in this way, the parallels between the principles of intergenerational equity and the types of considerations that company directors already take into account are clear. The inclusion of directors in climate change policy is logical, and justified by the theoretical underpinning provided by intergenerational equity.

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<sup>161</sup> Notwithstanding the fact that shareholders can, by special resolution, elect to have the company wound up: *Corporations Act 2001* (Cth) s 461(1)(a).

## VII INCORPORATION'S INHERENT COSTS

Despite the doctrine of separate corporate entity remaining largely unchanged for over a century, it is not universally accepted. A classic argument against the doctrine is that company managers, as handlers of other people's money rather than their own, cannot be expected to watch over it with the same anxious vigilance. In the words of Adam Smith, 'negligence and profusion must always prevail... in the management of such a company.'<sup>162</sup> This comes about because managers cannot enjoy all of the gains where a company is successful and they do not bear all the loss if a company fails. They have less incentive to maximise wealth than if they themselves were the owners.<sup>163</sup> This perspective suggests that corporate law serves as the only constraint on managerial behaviour as managers freed from legal constraints could easily abuse shareholders' interests without any cost to themselves.<sup>164</sup> Directors' duties are among the most powerful of all corporate laws as they dictate the standard of behaviour required of directors personally. Gross breaches of these duties can attract severe penalties, including imprisonment.<sup>165</sup>

### *A Mitigating Incorporation's Inherent Costs by Controlling Management Behaviour*

In order to mitigate the risks introduced by separating company ownership from control, a range of fiduciary and statutory duties are imposed on company directors. This imposition serves a social policy end as it seeks to protect shareholders from directors who might otherwise exploit the doctrine of separate entity for their own

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<sup>162</sup> Adam Smith, *The Wealth of Nations*, (Modern Library, 1776).

<sup>163</sup> Daniel R Fischel, above n 70, 1262-3.

<sup>164</sup> Harry N Butler, 'The Contractual Theory of the Corporation' 11 *George Mason University Law Review* 99, 102.

<sup>165</sup> For example, where there is an element of dishonesty or recklessness, a breach of s 181(1) can be a criminal offence: *Corporations Act 2001* (Cth) s 184(1). The penalty for such a breach is 2,000 penalty units or 5 years imprisonment or both: *Corporations Act 2001* (Cth) sch 3.

gain. In this way, directors' duties play a pivotal role in maintaining a balance between the benefits and risks brought by incorporation.<sup>166</sup>

Company directors are in a powerful position to assess and influence both the impact that the corporation has on the climate and also the impact the climate has on the corporation. This essay draws attention to the idea that ignoring the well documented adverse impacts that climate change can have on corporations<sup>167</sup> is arguably a breach of duty. By extension, it argues that directors' duties are well placed to play a role in a bottom up approach to climate change management. This is because directors' duties can serve to sharpen the focus on the potentially adverse economic impacts of climate change. In so doing, they provide a genuine incentive for managers and owners alike to support the inclusion of corporations in climate change mitigation policy.

### *1 Section 181 – The Duty to Act in the Best Interests of the Corporation*

Company directors are bound by a fiduciary duty to act honestly and in good faith in furthering the interests of the company as a whole.<sup>168</sup> The common law duty is bolstered by section 181 of the *Corporations Act*, which specifically imposes an obligation on directors to act in good faith in the best interests of the corporation and for a proper purpose. As fiduciaries, company directors are held to a very high standard of behaviour. In *Meinhard v Salmon*,<sup>169</sup> Cardozo CJ made what is widely accepted to be a leading statement on this expected standard of behaviour. He said that company directors are '...held to something stricter than the morals of the market

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<sup>166</sup> Of course, 'piercing the corporate veil' is a technique available to courts to remedy such actions, but discussion of that is outside of the scope of this essay. See, eg, Ian M Ramsay and David B Noaks, above n 75.

<sup>167</sup> John A Purcell and Janice A Loftus, above n 103; 'Bottom Up and Country Led: A New Framework for Climate Change Action', above n 49.

<sup>168</sup> *Corporations Act 2001* (Cth) s 181(1).

<sup>169</sup> *Meinhard v Salmon* 164 NE 545 (NY, 1928).

place. Not honesty alone, but the punctilio of an honor the most sensitive.’<sup>170</sup> This high standard can present a problem for some directors as the meaning of the ‘company as a whole’ as well as what constitutes a benefit for the company are the subject of lively debate. Both notions and their interpretations are relevant to this essay as directors making decisions with the interests of stakeholders other than shareholders in mind can wander into breach territory unless they can demonstrate a benefit for the company. Climate change’s unique special and temporal dimensions can make it difficult to demonstrate an immediate or tangible benefit.

(a) *Who is the Company?*

Traditionally, ‘the company as a whole’ is understood to be the owners, or shareholders as a collective group.<sup>171</sup> The concept is flexible though and what constitutes the interests of the company can depend on when the inquiry is made.<sup>172</sup>

While shareholders are generally considered to be the company, this cannot be taken to mean that directors must only consider shareholder interests when making decisions.<sup>173</sup> Indeed, James McConvill goes as far as saying taking stakeholder interests into consideration is inevitable when acting in the best interests of the company.<sup>174</sup> Not only is it now quite acceptable for directors to take into account the interests of other groups such as employees, recent case law indicates that directors *must* take into account the interests of other groups, mainly creditors.<sup>175</sup>

However, while courts have recognised that it sometimes is in the company’s best interests for directors to take into account the interests of groups other than

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<sup>170</sup> *Ibid.*.

<sup>171</sup> *Greenhalgh v Arderne Cinemas Ltd* [1951] Ch 286.

<sup>172</sup> *The Bell Group Ltd v Westpac Banking Corporation (No 9)* (2008) 39 WAR 1, [4393]-[4395].

<sup>173</sup> *Ibid.*

<sup>174</sup> James McConvill, ‘Directors Duties to Stakeholders: A Reform Proposal Based on Three False Assumptions’ (2005) 18(1) *Australian Journal of Corporate Law* 88.

<sup>175</sup> *The Bell Group Ltd v Westpac Banking Corporation (No 9)* (2008) 39 WAR 1.

shareholders, they have not expressly recognised stakeholder theory per se. Nevertheless, parallels can be drawn between the theory and recent judicial commentary. For example, a Canadian court recently stated that ‘...in determining whether [directors] are acting with a view to the best interests of a corporation it may be legitimate, given all the circumstances of a given case, for the board of directors to consider, inter alia, the interests of shareholders, employees, suppliers, creditors, consumers, governments and the environment.’<sup>176</sup> In Australia, in *The Bell Group Ltd (in liq) v Westpac Banking Corporation [No 9]* (*‘Bell’*), Owen J said,

...it does not follow that in determining the content of the duty to act in the interests of the company, the concerns of shareholders are the only ones to which attention need be directed or that the legitimate interests of other groups can safely be ignored.<sup>177</sup>

It is acknowledged that in the *Bell* case, it was creditors who were the non-shareholder stakeholder of primary concern, however, Owen J’s comments are sufficiently broad that they may be applied to other groups as well. It is thus established that what constitutes ‘the company as a whole’ is a broad concept which can include groups with an interest in the corporation’s activity, even where they do not own shares. This essay argues that in light of this, future generations and the climate are both stakeholders with legitimate interests in corporate activity who cannot safely be ignored by directors when making decisions and acting for the benefit of the company as a whole.

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<sup>176</sup> *People’s Department Stores Inc v Wise* (2004) 244 DLR 564, 46.

<sup>177</sup> *The Bell Group Ltd v Westpac Banking Corporation (No 9)* (2008) 39 WAR 1, [4395].

(b) *Where is the Benefit? An Element of Futurity*

The duty to act in the best interest of the corporation takes on another vagary in its notion of what constitutes a benefit. It is not uncommon for managers to adopt a far-sighted approach to corporate decision making which can result in, if not a detriment, then certainly a lack of any real benefit in the short term. This situation has been the subject of judicial review, with the court finding that directors can take a long term view of what is in the best interests of a corporation in order to ensure ongoing viability.<sup>178</sup> There is case law to support the view that directors are ideally placed to determine which actions are in the best interests of the company, and that they have a great deal of discretion in doing so.<sup>179</sup> Addressing this point, the High Court has said,

[d]irectors... may be concerned with a wide range of practical considerations, and their judgment, if exercised in good faith and not for irrelevant purposes, is not open to review in the courts.<sup>180</sup>

In other words, provided that directors are making decisions where it is conceivable that the company will benefit, they may adopt a long-term view in their decision making without risking breaching their duties. Permitting managerial decisions which delay corporate benefit is sensible given the ongoing nature of most corporations, and that most shareholders expect current as well as future interests to be considered, as discussed above.

There is some judicial commentary that would seem to indicate that not only are the future interests of current shareholders worthy of consideration, but so are the interests of future shareholders. In *Darvall v North Sydney Brick & Tile Co Ltd (No*

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<sup>178</sup> *Darvall v North Sydney Brick & Tile Co Ltd (No 2)* (1989) 6 ACLC 154.

<sup>179</sup> *Ibid*; *Strong v J Brough & Son (Strathfield) Pty Ltd* (1991) 9 ACLC 1018; *Automatic Self-Cleansing Filter Syndicate Co v Cunningsham* [1906] 2 Ch 34; *John Shaw & Sons (Salford) Ltd v Shaw* [1935] 2 KB 113.

<sup>180</sup> *Harlowe's Nominees Pty Ltd Woodside (Lakes Entrance) Oil NL* (1967) 121 CLR 483, 493.



2), Hodgson J said, ‘...it is proper to have regard to the present and future members of the company, on the footing that it would be continued as a going concern.’<sup>181</sup> This and other judicial commentary<sup>182</sup> indicates that the element of futurity in this duty applies not only to the company’s future interests, but also to the interests of future shareholders.<sup>183</sup> By taking into account the interests of future shareholders, directors acknowledge the interests of the company as a distinct commercial entity, separate from the short-term interests of its current shareholders.<sup>184</sup>

The fact that directors are accustomed to dealing with notions of futurity is critical to this essay’s argument. This essay proposes an extension of the consideration of the future interests of current or future shareholders to the interests of future generations, regardless of their shareholder status. Part of the reason why directors’ duties have been identified as the appropriate legal tool for inclusion in a bottom up approach is their demonstrated ability to successfully incorporate notions of futurity into corporate decision making.

## 2 Section 180 – *The Duty to Act With Care, Skill and Diligence*

Section 180 of the *Corporations Act* requires that company directors exercise their powers with the degree of care and diligence that a reasonable person would exercise if they were a director or officer of a company in the company’s circumstances; and

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<sup>181</sup> (1989) 6 ACLC 154, 554.

<sup>182</sup> *Provident International Corp v International Leasing Corp Ltd* [1969] 1 NSW 424, 440 per Helsham J; *Gaiman v National Association for Mental Health* [1971] Ch 317, 330 per Megarry J.

<sup>183</sup> It is accepted that this idea is perhaps at odds with the fact that shareholders can move to wind the company up: *Corporations Act 2001* (Cth) s 461(1)(a). However, it can be said that in all but exceptional cases, it will be very much in the interests of current shareholders for the directors to make decisions with a long term view in mind. It has been suggested that these two points of view can be reconciled by the idea that the duty of directors is not so much to take into account the interests of future members as it is to act for the benefit of existing members while having regard to their future interests. See, eg. Ian Renard, ‘Directors’ Duties and the Company’s Interests’ in Paul Finn (ed), *Equity and Commercial Relationships* (The Law Book Company Ltd, 1987) 138; L C B Gower, ‘Corporate Control: The Battle for The Berkeley’ (1955) 68(7) *Harvard Law Review* 1176, 1184.

<sup>184</sup> J Dyson Heydon, ‘Directors’ Duties and the Company’s Interests’ in Paul Finn (ed), *Equity and Commercial Relationships* (The Law Book Company Ltd, 1987) 120, citing *Peters American Delicacy Co Ltd v Heath* (1939) CLR 457, 480 per Latham CJ.

occupied the office held by, and had the same responsibilities within the company as, the director or officer.<sup>185</sup> The purpose of section 180 is not to punish directors every time they make an error of judgment. Rather, it is to set a standard by which the proper taking of risk in making business decisions can be measured.<sup>186</sup> This duty founds an argument that not only must directors be attuned to the potential impact known risks could have on their companies, but they are obliged to take positive steps to mitigate any damage that may occur. It is argued that climate change now unequivocally has the status of a known risk with potentially serious consequences for corporations. A report by Booz and Company into the impact of climate change on business identified six ways climate change can impact economic activity. The report listed these as:

1. The global economy is both directly and indirectly linked to the earth's climate system.
2. Sectors such as tourism, agriculture and insurance are directly affected by increased adverse climate conditions.
3. Emissions must be reduced if climate change is to be managed and mitigated.
4. Other sectors will also be impacted, including the energy sector. This will see a flow-through effect to other, energy-intensive sectors such as mining and manufacturing.
5. Other direct impacts include reduced demand for products, disruption to business activities, potential litigation, as well as brand and reputational risk.
6. Longer-term global impacts could include large-scale refugee movement, political instability and social unrest.<sup>187</sup>

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<sup>185</sup> *Vrisakis v ASIC* (1993) 9 WAR 395; *Australian Securities Commission v Gallagher* (1993) 11 WAR 105; *Daniels v Anderson* (1995) 37 NSWLR 438.

<sup>186</sup> *Australian Securities and Investments Commission v Lindberg* (2012) 91 ACSR 640, [68]-[73].

<sup>187</sup> KPMG Australia, above n 50.

Given this, it is argued that directors who fail to take reasonable steps to address the potential adverse impacts of climate change could conceivably be in breach of their duty to discharge their powers with due care and diligence and in the best interests of the corporation. Taking steps to build corporate resilience to the threats brought by climate change is not the same as taking steps to actively reduce a corporation's GHG emissions. Under the current law, while a director could be found to have breached his or her duties by failing to take steps to protect the corporation from foreseeable climate change related harm, they would unlikely be found to be in breach simply because their company was not actively contributing to a reduction in GHG emissions. This is why a new duty that does impose such an obligation is required if corporations are going to form a key part of a new, bottom up approach to effective climate change mitigation. An effective and innovative way of achieving this is to make the climate and future generations the subject of a new directors' duty.

## VIII CORPORATE SOCIAL RESPONSIBILITY

It is appropriate to examine the significance of ‘corporate social responsibility’ (CSR). CSR has been defined by the Corporations and Markets Advisory Committee (CAMAC) as the extent to which companies do, or should, take into account the environmental and social impacts of their activities.<sup>188</sup> Standards Australia defines CSR as ‘a mechanism for entities to voluntarily integrate social and environmental concerns into their operations and their interaction with their stakeholders, which are over and above the entities’ legal responsibilities.’<sup>189</sup> John Parkinson provides a more detailed explanation of CSR and its role in company decision making. He says CSR is

[b]ehaviour that involves voluntarily sacrificing profits, either by incurring additional costs in the course of the company’s production processes, or by making transfers to non-shareholder groups out of the surplus thereby generated, in the belief that such behaviour will have consequences superior to those flowing from a policy of pure profit maximisation.<sup>190</sup>

Although there is some research that suggests companies with reputations for being socially responsible do perform better, the research as a whole has produced conflicting results.<sup>191</sup> Nevertheless, some studies have been compelling. For example, in a 2007 study, researchers selected 30 companies that adopted a ‘managing for stakeholders’ approach – that is, companies who treated stakeholders

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<sup>188</sup> Corporations and Markets Advisory Committee, Parliament of Australia, *The Social Responsibility of Corporations* (2006)  
<[http://www.camac.gov.au/camac/camac.nsf/byHeadline/PDFFinal+Reports+2006/\\$file/CSR\\_Report.pdf](http://www.camac.gov.au/camac/camac.nsf/byHeadline/PDFFinal+Reports+2006/$file/CSR_Report.pdf)>.

<sup>189</sup> Standards Australia, ‘Corporate Governance – Corporate Social Responsibility’ (2003) AS 8003-2003.

<sup>190</sup> John E Parkinson, *Corporate Power and Responsibility: Issues in the Theory of Company Law* (Clarendon Press, 1995) 260-261.

<sup>191</sup> Karina Funk, above n 96; Tobias Hahn et al, ‘Trade offs in Corporate Sustainability: You Can’t Have Your Cake and Eat It’ (2010) 19 *Business Strategy and the Environment* 217.

far more generously than legal obligations required. These companies were shown to significantly outperform the Standard and Poor's 500 over both short- and long-term timeframes.<sup>192</sup> Another study of over 500 companies over a period of 11 years suggests, unsurprisingly, that firms with good stakeholder relations sustain superior performance. What was interesting in this study was that it indicated that firms with strong stakeholder relationships also recovered more quickly from disadvantageous positions.<sup>193</sup>

Themes of voluntariness and ideas of what corporations 'should' or 'ought' to be doing run strong in the CSR literature. The movement has never completely reconciled with the economic theory of firms and for this reason remains a corporate 'nice to have' rather than a compulsory aspect of corporate governance. Critics of the CSR movement argue that because it is entirely voluntary, most CSR efforts result in little more than 'green washing' or 'box ticking'.<sup>194</sup> That is, they are undertaken more for show than to achieve any real impact on social or environmental ills. It is true that industry will often commit to voluntary codes of practice in order to avoid stricter and enforceable legal regulation.<sup>195</sup> David Engel sums this up succinctly:

It seems... that the basic question of corporate social responsibility is not whether we wish to compel or forbid certain kinds of corporate conduct by legislative command... but rather whether it is socially desirable for corporations organised for profit voluntarily to identify and pursue social ends

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<sup>192</sup> Rajendra S Sisodia, David B Wolfe and Jagdish Sheth, *Firms of Endearment: How World-Class Companies Profit from Passion and Purpose* (Pearson Education India, 2007).

<sup>193</sup> Jaepil Choi and Heli Wang, 'Stakeholder Relations and the Persistence of Corporate Financial Performance' (2009) 30(4) *Strategic Management Journal* 895.

<sup>194</sup> Ronen Shamir, 'Capitalism, Governance and Authority: The Case of Corporate Social Responsibility' (2010) 6 *Annual Review of Law and Social Science* 531; Denise A Braden, Ian A Harwood and David G Woodward, 'The Effect of Buyer Pressure on Suppliers in SMEs to Demonstrate CSR Practises: An Added Incentive or Counter Productive?' (2009) 27(6) *European Management Journal* 429; James A H S Hine and Lutz Preuss, 'Society is Out There, Organisation is in Here': On the Perceptions of Corporate Social Responsibility Held by Different Managerial Groups' (2008) 88 *Journal of Business Ethics* 381.

<sup>195</sup> David Vogel, above n 52.

where the pursuit conflicts with the presumptive shareholder desire to maximise profit.<sup>196</sup>

This observation is important to this essay's thesis because many company directors have adopted practices founded in CSR to reduce or manage their contribution to climate change.<sup>197</sup> It is argued that this has to change as climate change is too important an issue to be left to voluntary undertakings and that CSR measures alone are insufficient to form the basis of corporate involvement in an effective climate change mitigation. Although CSR is not identified as an effective way to mitigate climate change, its wide acceptance by the business community shows that companies and their directors do have the inclination and resources to adopt practices that are better for groups who are not shareholders without unduly sacrificing their profit goals. This essay argues that Parliament needs to identify and select the values and groups which are worthy of compulsory consideration by directors, rather than leaving it to profit-oriented firms to do so. In this way the interests of future generations and the climate itself can be consistently and effectively upheld through a positive, non-voluntary duty.

### *A Stakeholder Theory and Corporate Social Responsibility*

CSR and stakeholder theory are often discussed in conjunction although they are quite distinct.<sup>198</sup> Donna Wood's research in this area is most useful in explaining the differences between the two concepts. Her work clearly formulates the idea that CSR challenges the purpose of a corporation, while stakeholder theory develops an approach to strategic management that acknowledges the need for the ongoing

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<sup>196</sup> David L Engel, 'An Approach to Corporate Social Responsibility' (1979-1980) 32 *Stanford Law Review* 1, 3.

<sup>197</sup> Douglas G Cogan, above n 60.

<sup>198</sup> Karina Funk, above n 96; Tobias Hahn et al, above n 191.

support of specific stakeholder groups.<sup>199</sup> Stakeholder theory is grounded in the idea that corporations rely on the support of many stakeholders who are not shareholders, and that maintaining positive relationships with these stakeholders is crucial for ongoing survival. CSR, on the other hand, is more about diverting corporate resources to social need in order to improve reputation which will then lead to improved corporate performance.<sup>200</sup>

*B Corporate Social Responsibility and Directors' Duties – The Parliamentary  
Inquiries*

The interface between directors' duties and CSR has recently been the subject of review in several countries.<sup>201</sup> The reviews came about for two reasons: First, as a response to the alleged abuse of the corporate form, and second in order to examine contemporary community expectations as to the role, if any, corporations should play in redressing social and environmental issues. In Australia, the CSR movement was the subject of two inquiries in 2005. Parliament referred to CAMAC a number of questions concerning the role of corporations in Australian society. CAMAC was specifically asked to assess whether, given the significant and broad impact of corporate activity in modern society, the Australian legal framework should allow or require directors to take into account the interests of stakeholders other than shareholders.<sup>202</sup> After seeking submissions and reviewing the current legal framework, CAMAC released a report, *The Social Responsibility of Corporations*,

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<sup>199</sup> See eg. Donna J Wood, 'Corporate Social Performance Revisited' (1991) 16(4) *Academy of Management Review* 691; Donna J Wood and Jeanne M Logsdon, 'Theorising Business Citizenship' in Jorg Andriof and Malcom McIntosh (eds), *Perspectives on Corporate Citizenship* (Greenleaf Publishing, 2001) 83.

<sup>200</sup> Karina Funk, above n 96.

<sup>201</sup> Australia, the United Kingdom, Singapore, Hong Kong and Malaysia have all recently undertaken reviews of general corporate law and also of directors' duties in particular. All these reviews have specifically included corporate social responsibility issues in their terms of reference.

<sup>202</sup> Corporations and Markets Advisory Committee, above n 188.

which recommended that no changes be made.<sup>203</sup> Similarly, the Parliamentary Joint Committee (PJC) on Corporations and Financial Services report, *Corporate Responsibility: Managing Risk and Creating Value* recommended no changes to directors' duties be made.<sup>204</sup>

While some argue that the inquiries recommended no changes be made because no change is warranted, this essay views these inquiries as lost opportunities to update Australian corporate law to allow corporations to play a role in effective climate change management. Perhaps, though, it is not surprising that the inquiries' potential to play a role in climate change policy was overlooked. Both were undertaken at a time before climate change as a global issue crystallised in Australian consciousness,<sup>205</sup> and prior to the introduction of the climate law package<sup>206</sup> which greatly increased awareness of the problems brought by climate change. Also, it is only fair to point out that, although 'the environment' was included in the terms of reference for the CAMAC inquiries, climate change was not.<sup>207</sup> The terms of reference for the PJC inquiry referred only to 'stakeholders other than shareholders, and the broader community'.<sup>208</sup>

The arguments presented by the committees against changing the *Corporations Act* were in response to issues related to CSR, not climate change. While much has been

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<sup>203</sup> Ibid.

<sup>204</sup> Parliamentary Joint Committee on Corporations and Financial Services, Parliament of Australia, *Corporate Responsibility: Managing Risk and Creating Value* (2006) <[http://www.aph.gov.au/binaries/senate/committee/corporations\\_ctte/completed\\_inquiries/2004-07/corporate\\_responsibility/report/report.pdf](http://www.aph.gov.au/binaries/senate/committee/corporations_ctte/completed_inquiries/2004-07/corporate_responsibility/report/report.pdf)>.

<sup>205</sup> Tim Bonyhady and Peter Christoff, *Climate Law in Australia* (Federation Press, 2007). According to Bonyhady and Christoff, 2006 was the year in which climate change matured into an issue of significant public and political concern.

<sup>206</sup> The first climate change-specific bill, the *Climate Change Action Bill 2006*, was introduced to the Senate on 30 November 2006.

<sup>207</sup> Corporations and Markets Advisory Committee, above n 188, 3-4.

<sup>208</sup> Parliamentary Joint Committee on Corporations and Financial Services, above n 204, vii.



written about the role CSR could play in climate change policy,<sup>209</sup> there is a paucity of research into how corporate law might be harnessed to form the basis of a bottom up approach to effective climate change mitigation. In light of this, this essay calls for a new re-examination of Australian corporate law and its potential to play a part in climate change mitigation.

Advocates of the stakeholder model argue that the *Corporations Act* should be changed to more clearly permit directors to take into account the interests of non-shareholder stakeholders. Stronger advocates argue for a change that would *require* directors to do so. There is concern that the current generalised flexibility in the duty to act in the best interests of the corporation could lead to directors being found to be in breach of their duties where they have taken into account the interests of non-shareholder stakeholders.<sup>210</sup>

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<sup>209</sup> See, eg, Investor Responsibility Research Centre, above n 7; Ans Kolk and Jonatan Pinkse, above n 7; Shameek Konar and Mark A Cohen, 'Does the Market Value Environmental Performance?' 83 *The Review of Economics and Statistics* 281.

<sup>210</sup> Shelley Marshall and Ian Ramsay, above n 226; John A Purcell and Janice A Loftus, above n 103.

## IX DIRECTORS' DUTIES – THE KEY TO INSTALLING CORPORATIONS IN A BOTTOM UP APPROACH TO MITIGATING CLIMATE CHANGE

Up until now, corporate impact on the environment has been controlled by specifically drafted legislation.<sup>211</sup> While this legislation has been effective as a tool to mitigate tame environmental problems, it can only go so far. It is argued here that the *Corporations Act* and in particular directors' duties are appropriate tools to regulate the impact of corporations on climate change. Shifting the focus to company directors and corporate decision making via the imposition of a duty to take into account the interests of the climate and future generations achieves a number of things the governance of wicked problems demands: It allows for creative, 'clumsy' solutions, access to established and well understood enforcement mechanisms and also puts the onus on company directors as people who are suitably skilled and well equipped to deal with wicked problems.

This essay does not purport to argue that shareholders, via the corporations they invest in, are responsible for directly funding the development and implementation of climate policy. Rather it argues that incorporation, the *Corporations Act*, and directors' duties in particular could be effective legal tools in the management of climate change. Directors' duties in particular have been used for many years to protect shareholders in their capacity as a group with an interest in corporate activity, but no right or ability to control corporate decision making. This essay argues that the interests of future generations and the climate should be afforded similar protections under corporate law.

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<sup>211</sup> For example, at the Commonwealth level the *Environmental Protection and Biodiversity Conservation Act 1999* (Cth), the *Climate Change and Greenhouse Gas Reduction Act 2010* (Cth) and, at a state level, the *Contaminated Sites Act 2003* (WA).

### *A The Corporations Act as a Moral Compass?*

In the past, shareholders were the only group offered protection by corporate law. However, because they effectively control almost all of society's resources, corporations are inevitably the axis of almost all of society's woes. Over time, this has led to other groups such as creditors and employees gaining some, albeit limited, protections under the *Corporations Act*. The history of the corporate form, outlined in part IV, shows how corporations were born of social need and thus very often the arena for the most pressing of social issues: Continuous ownership of private property presented a need for an ongoing entity<sup>212</sup> and exploring the new world introduced a need for an entity that could spread risk more widely.<sup>213</sup> In more recent times, labour rights, and anti-discrimination and equal opportunity movements are also examples of problems of huge importance to the community that have played out in the corporate arena. The example of employee rights and protections is particularly illustrative here. In 1932 Dodd observed that

[r]ecent economic events suggest that the day may not be far distant when public opinion will demand a much greater degree of protection to the worker. There is a widespread and growing feeling that industry owes to its employees not merely the negative duties of refraining from overworking or injuring them, but the affirmative duty of providing them so far as possible with economic security.<sup>214</sup>

Not even one hundred years later a sophisticated employment relations system, strict liability occupational safety and health laws, unfair dismissal regimes, overtime rates and paid parental leave make that statement laughable. This clearly shows how

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<sup>212</sup> Phillip Lipton, Abe Herzberg and Michelle Walsh, *Understanding Company Law* (Law Book Co, 15<sup>th</sup> ed, 2010), 4.

<sup>213</sup> Samuel Williston, above n 66.

<sup>214</sup> E Merrick Dodd, above n 78, 1151.

quickly social attitudes towards the role of corporations in society can change, and, critically, how well corporations themselves do adapt to such change. Indeed, today, cultivating a reputation as an ‘employer of choice’ is viewed as essential to maintaining a competitive advantage, and firms are quick to point to their safety records, benefits packages and equal opportunity credentials when selling themselves to potential investors and employees.

At the birth of corporate law as we know it today, the interests of shareholders were paramount. The longevity of legislation enshrining this value is testament to the importance of security of investment to the community. Stable, successful and profitable businesses are what the community needs. Legal steps were rightly taken to ensure that shareholders could invest, safe in the knowledge that their interests were protected by robust legal tools and that courts would not hesitate to intervene where necessary.<sup>215</sup>

The commercial arena is now grappling with the questions brought by climate change. Our understanding of our relationship with the environment and the climate is constantly changing, and practices that were once thought to be acceptable and ethical may not withstand current social attitudes. Because companies are the largest emitters of GHG, in order for them to maintain the legitimacy and privilege incorporation affords, they need to become an active participant in climate change mitigation. This essay argues that corporations need to be better enabled to do so, and that a change to current corporate law is required. It argues that a duty to take into account the interests of future generations and the climate as well as shareholders will enable the active corporate participation required. The principles of

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<sup>215</sup> This is not to suggest that courts will intervene to ensure shareholders get a return. It is acknowledged that courts will not interfere with business decisions unless an action is properly brought and it is clear a breach has occurred.

intergenerational equity, outlined in part VI, are called upon to develop this duty in a manner that does not unfairly impact current shareholders.

### *B Enforcing the License to Operate*

Corporate law, and directors' duties in particular, are no more than social values in legislated form. Directors' duties represent Parliament's acknowledgment of the far-reaching and significant impact corporations have on modern society. Because corporations are managed by self-interested human beings, some regulation is required to ensure this impact is controlled. Directors' duties have proven to be an effective and popular legal mechanism for ensuring corporations fulfil their side of the social bargain entered into upon incorporation. They set the standards of behaviour required to ensure that the benefits of incorporation flow as freely and fairly as possible. The duties' popularity and effectiveness comes about from their enforceability and also from their ability to deal ably with the many grey areas in human decision making and business judgment.<sup>216</sup>

This is an important point – making business decisions is difficult, and always involves a weighing of risk. It is accepted that not every business decision will lead to a benefit for the company but that lack of benefit does not prove lack of good faith or due care and skill. Company directors are expected to take calculated commercial risks. A company run on the basis that no risks were ever taken would be unlikely to be successful. For this reason courts are rightly reluctant to interfere in business decision making. The business judgment rule, provided in section 180(2) of the *Corporations Act* is in essence the community's acknowledgment that sometimes, in the 'fog of commerce,' directors will take action that turns out not to be in the best

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<sup>216</sup> Ngozi Okoye, 'The Personality of Company Directors and Behavioural Risks in Corporate Governance: Bridging the Unidentified Gap' (2013) 10 *International Journal of Disclosure and Governance* 261.

interests of the company. For there to be a case against the company director, elements of bad faith, irrationality or unreasonableness are required.<sup>217</sup> The new duty proposed by this essay would include a similar type of defence.

John Purcell and Janice Loftus note how common it is for debate in this area to be dismissed as politicking.<sup>218</sup> Discussion about the social bargain that is incorporation can quickly be derailed by declarations that run on strictly politically left or right lines. In reality, the issue is far more nuanced and really about how corporations affect the community. Purcell and Loftus agree with Parkinson's suggestion that adopting the view that corporations, in particular large corporations, are social enterprises<sup>219</sup> as a way to avoid this derailment. In this way, legitimate exercising of corporate decision-making power can be assessed from the perspective of a wider public interest.

While he is careful to point out that the corporate form as we know it today may quite likely be 'the most conducive to the public good,'<sup>220</sup> Parkinson still asserts that because corporations are social bodies, albeit under private control, their directors should be held to the same standards of conduct as those holding public office.<sup>221</sup> This is because for a number of sectors and most large corporations, the contemporary reality is a degree of market concentration that affords corporations the ability to pass on the cost of social expenditure to customers.<sup>222</sup> This essay asserts that by virtue of the power they hold, directors must be held more accountable for the

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<sup>217</sup> For a full discussion of the business judgment rule and its application by the courts, see Jenifer Varzaly, 'Protecting the Authority of Directors' An Empirical Analysis of the Statutory Business Judgment Rule' (2012) 12 *Journal of Corporate Law Studies* 429.

<sup>218</sup> John A Purcell and Janice A Loftus, above n 103, 139.

<sup>219</sup> Parkinson, above n 190, 24.

<sup>220</sup> Ibid.

<sup>221</sup> Ibid.

<sup>222</sup> John A Purcell and Janice A Loftus, above n 103, 140.

impact their corporations have on the climate and the community. This is not to further a conservationist cause, but rather to ensure that the effects of climate change can be managed such that all generations can enjoy the economic benefits of incorporation.

### *C Why is a Change to Current Directors' Duties Required?*

As discussed in part VII, there is widespread acknowledgment that Australian corporate law, particularly the duty to act in the best interests of the company, has enough built-in flexibility to allow directors to adopt something of a stakeholder approach.<sup>223</sup> Despite this acknowledgment there is still doubt among company directors about whether they would completely escape liability if they deliberately adopted a stakeholder approach to company management.<sup>224</sup> This is because there has to date been no explicit judicial sanction of the stakeholder concept. Shelley Marshall and Ian Ramsay compare the writings of Ross Parsons and Leonard Sealy to illustrate this development.<sup>225</sup> Writing of Australian cases decided between 1889 and 1962 and examining the duty to act in the best interest of the corporation,<sup>226</sup> Parsons concludes that the interests of employees, consumers, creditors, debenture holders and the public 'do not enter the calculation.'<sup>227</sup> Writing but twenty years later, Sealy interprets the law as allowing the consideration of non-shareholder stakeholders' interests – but only to the extent that shareholders would enjoy a 'derivative benefit.'<sup>228</sup> This indicates that the judiciary has been influenced by some

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<sup>223</sup> Robert P Austin and Ian Ramsay, *Ford's Principles of Corporations Law* (LexisNexis Butterworths, 14<sup>th</sup> ed, 2010) [8.020], [8.020]-[8.150].

<sup>224</sup> John A Purcell and Janice A Loftus, above n 103, 142-145; Shelley Marshall and Ian Ramsay, above n 226, 295-299.

<sup>225</sup> Shelley Marshall and Ian Ramsay, above n 226, 297-298.

<sup>226</sup> *Re William Brooks & Co Ltd and the Companies Act* (1962) 79 WN (NSW) 354; *Richard Brady Franks Ltd v Price* (1937) 58 CLR 112; *Re Atlas Engineering Company* (1887) 10 LR (NSW) Eq 179.

<sup>227</sup> Ross W Parsons, 'The Directors' Duty of Good Faith' (1967) 5 *Melbourne University Law Review* 395, 418.

<sup>228</sup> Len S Sealy, 'Directors' 'Wider' Responsibilities – Problems Conceptual, Practical and Procedural' (1987) 13 *Monash University Law Review* 164, 187.

of the principles of stakeholder theory and is starting to acknowledge the community acceptance, or even expectation, of corporations playing a wider social role.

Twenty years later again, Owen J, in *Bell*, weighed in on the issue. Here, Owen J states that it is incorrect to treat shareholders and the company as a whole as the same thing in all circumstances, and that there are a number of factors that should be taken into account when determining what or who ‘the company’ is in any given case. These factors include the particular context, type of company and nature of the directors’ activity.<sup>229</sup> Furthermore, Owen J made it clear that where solvency may be an issue, directors are in fact obliged to take into account the interests of creditors.<sup>230</sup> However, His Honour then went on to say that it should not be taken as a rule that in these situations the interests of creditors are paramount.<sup>231</sup> It is no surprise, then, that there is still doubt among company directors about whose interests they can legitimately take into account when making decisions.

Although the above analysis of decisions in the area does indicate growing judicial acceptance of a widening of what constitutes acting in the best interests of the corporation, it would be a brave director who tests this ground. Indeed, Marshall and Ramsay conclude unequivocally that the question of in whose interests directors of Australian companies should act is one which has not been settled satisfactorily.<sup>232</sup> This doubt would certainly be increased if the stakeholders in question were in the abstract – for example, the climate or future generations. It is contended here that the current state of Australian corporate law could not form the basis for engaging corporations in a bottom up approach to climate change mitigation because of the

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<sup>229</sup> *The Bell Group Ltd (in liq) v Westpac Banking Corporation [No 9]* (2008) 39 WAR 1.

<sup>230</sup> *Ibid*, 540.

<sup>231</sup> *Ibid*, 544-545.

<sup>232</sup> Shelley Marshall and Ian Ramsay, above n 226, 312.



uncertainty about how far directors could go in considering the interests of stakeholders such as future generations or the climate.

### *1 Empirical Evidence of Current Practice*

One of the difficulties with assessing how much flexibility should be permitted within directors' duties is that it is almost impossible to know what directors are thinking when they make decisions. Shareholders are generally not permitted access to meeting minutes,<sup>233</sup> and publicly available information does not usually disclose detailed reasoning behind corporate decisions. In an attempt to better understand the motivations behind corporate decision making, Marshall and Ramsay undertook empirical research into what directors understand their duties to be and whether the law is out of step with current boardroom practice. They sought to discover whether imposing a legal requirement that directors take into account the interests of stakeholders or taking the lesser step of permitting them to do so would amount to a genuine re-conceptualisation of 'in whose interests the company operates' or merely bring the law in line with current practice.<sup>234</sup> In their research, they note that neither the CAMAC nor the PJC inquiries had access to any such evidence and so were unable to know if any change in the law would actually amount to a change in practice. This calls into question some of the support for the committees' findings.<sup>235</sup>

Marshall and Ramsay's results were revealing. They found that 55 per cent of directors believe that acting in the best interests of the company means balancing the interests of all stakeholders, and that 38.2 per cent believe it means acting in the

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<sup>233</sup> Minutes of directors' meetings are generally not available to members: *Corporations Act 2001* (Cth) s 251B.

<sup>234</sup> Shelley Marshall and Ian Ramsay, above n 226.

<sup>235</sup> See, eg, McConvill, above n 174; John A Purcell and Janice A Loftus, above n 103; Aiman Nariman Mohd-Sulaiman, 'Internalising Corporate Social Responsibility (CSR) - Looking Beyond Directors' Duties' (2011) 7(13) *Journal of Applied Science Research* 2411.

interests of all stakeholders to achieve the long-term interests of shareholders. Only 5.7 per cent of directors believed the *Corporations Act* imposed a requirement to take into account only shareholders' interests. Marshall and Ramsay concluded that despite a lack of express judicial approval, Australian corporate law as it stands is consistent with a stakeholder approach, albeit in a limited sense. In their view, directors are not permitted to treat the discharge of stakeholder interests as an end in itself but may take into account the interests of non-shareholder stakeholders where it can be argued that shareholders will benefit as well.<sup>236</sup>

Marshall and Ramsay found that directors look to business imperatives and ethics for guidance concerning the interests they should consider, not corporate law.<sup>237</sup> This indicates that the duty proposed by this essay would make very little practical difference to the way directors approach corporate governance, but it would introduce clarity and bring the law in line with reality. In addition, it would legitimise the abstract concepts of future generations and the climate as corporate stakeholders. Such a change would also make a real contribution to the way the detrimental effects of climate change are managed and mitigated. This essay does not advocate that shareholders' interests simply be secondary to other stakeholders', far from it – instead, it calls for a re-examination of how theories of firm organisation benefit and impact society. The argument in this essay looks to stakeholder theory for guidance on how to accommodate competing interests to ensure firm survival, and to intergenerational equity to craft a directors' duty that ensures the economic benefits of incorporations are not lost and are able to be enjoyed by all generations.

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<sup>236</sup> Shelley Marshall and Ian Ramsay, above n 226, 299.

<sup>237</sup> *Ibid.*

### D Why Directors' Duties Over Other Forms of Regulation?

There are strong arguments against modifying directors' duties in order to achieve social and environmental goals. They deal primarily with the flexibility already provided by the law,<sup>238</sup> vagueness inherent in the language of CSR<sup>239</sup> and question the logic behind an institution set up for profit being expected to identify and redress social misery.<sup>240</sup> These are valid arguments, and it is agreed that directors' duties are a poor choice of legal tool if increased CSR is the goal, but this essay is not about improving a corporation's CSR credentials. Rather, it is about developing an approach to climate change that forces decision making down to lower levels – levels closer to where GHG emissions originate, and levels where effective bottom up management of a wicked problem can take hold.

We turn here again to Barrett's three features of a successful regulatory instrument. For an instrument to be effective it must attract broad participation, it must ensure compliance, and it must do both these things while asking parties to change their behaviour.<sup>241</sup> It is argued that directors' duties are capable of all three of Barrett's outcomes. They attract broad participation by targeting corporations, not just selected emitters. The enforcement of directors' duties is well understood, established and accepted. Finally, the proposed duty would force a change in behaviour by imposing a duty on directors to consider other interests in their decision making. Thus it is

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<sup>238</sup> John A Purcell and Janice A Loftus, above n 103.

<sup>239</sup> Deryn Fisher, 'The Enlightened Shareholder - Leaving Stakeholders in the Dark: Will Section 172(1) of the Companies Act 2006 Make Directors Consider the Impact of Their Decisions on Third Parties?' (2009) 20(1) *International Company and Commercial Law Review* 10; Andrew Keay, 'Shareholder Primacy and the Advent of Enlightened Shareholder Value in the Reform of Directors' Duties in the United Kingdom' (Paper presented at the Corporate Law Teachers Association Annual Conference, University of Queensland, Brisbane, Queensland, 2006).

<sup>240</sup> Margolis and Walsh, above n 100; Lisa M Fairfax, 'Doing Well While Doing Good: Reassessing the Scope of Directors' Fiduciary Obligations in For-Profit Corporations with Non-Shareholder Beneficiaries' (2002) 59 *Washington and Lee Law Review* 409.

<sup>241</sup> Scott Barrett, above n 27, 2.

argued that where the end goal is climate change mitigation, directors' duties, rather than other forms of legal regulation, are ideally suited to play a role.

### E *The United Kingdom Example*

While this essay joins the chorus of those calling for a major rethink in the way climate change is managed,<sup>242</sup> it is somewhat lonely in its proposal to use directors' duties as a way to do so. However, the proposed duty is not as radical as it may first appear. Not only have the changes proposed here been discussed for many years by many commentators (albeit in a more general CSR, non-climate change related context), but a change similar to the one proposed here has already been instituted in the UK. While this change was not introduced with climate change mitigation in mind, it nevertheless demonstrates that significant changes to corporate law are not out of the question. After a review by the Company Law Review Group, the Companies Act 2006 (UK) ('*Companies Act*') was introduced to specifically address the issue of what constitutes the interests of the company. Section 172(1) of the *Companies Act* provides that in carrying out their duty to act in the best interests of the company as a whole, directors are required to have regard to, inter alia, the likely consequences of any decision in the long term and the impact of the company's operations on the community and the environment.<sup>243</sup>

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<sup>242</sup> Prins et al, above n 1; Rayner and Prins, above n 1; Prins and Rayner, above n 39.

<sup>243</sup> Section 172(1) of the *Companies Act 2006* (UK) reads:

172 Duty to promote the success of the company

- (1) A director of a company must act in the way he considers, in good faith, would be most likely to promote the success of the company for the benefit of its members as a whole, and in doing so have regard (amongst other matters) to—
- (a) the likely consequences of any decision in the long term,
  - (b) the interests of the company's employees,
  - (c) the need to foster the company's business relationships with suppliers, customers and others,
  - (d) the impact of the company's operations on the community and the environment,
  - (e) the desirability of the company maintaining a reputation for high standards of business conduct, and
  - (f) the need to act fairly as between members of the company.

The Explanatory Note to the Companies Bill 2006 (UK) states that while the list is not exhaustive, it is meant to highlight areas of particular importance which reflect the wider community's expectations of acceptable corporate behaviour.<sup>244</sup> Once again, we see directors' duties in action as the guardians of social values, and corporate law being used to ensure the benefits of incorporation are enjoyed by more than just the shareholders. Section 172(1) of the *Companies Act* does not operate to compromise shareholder interests. What it does do is require directors to consider the interests of a wider group of stakeholders as part of a duty to promote the success of the company.

It is noted here that several states in the United States of America have legislated to permit, but not require, directors to take into account interest of groups other than shareholders when executing their powers.<sup>245</sup> Because this legislation provides only statutory permission to consider the interests of stakeholders other than shareholders rather than take the stronger step of requiring it, it is not examined in any detail here.

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- (2) Where or to the extent that the purposes of the company consist of or include purposes other than the benefit of its members, subsection (1) has effect as if the reference to promoting the success of the company for the benefit of its members were to achieving those purposes.
  - (3) The duty imposed by this section has effect subject to any enactment or rule of law requiring directors, in certain circumstances, to consider or act in the interests of creditors of the company.

<sup>244</sup> Companies Bill 2006 (UK), Explanatory Note 308–9.

<sup>245</sup> For a discussion on the implications of this legislation, see, eg, Eric W Ortz, 'Beyond Shareholders: Interpreting Corporate Constituency Statutes' (1992) 61 *George Washington Law Review* 14; Eric W Ortz, 'Shirking and Shaking: A Legal Theory of the Firm' (1998) 16(2) *Yale Law and Policy Review* 265; Lisa M Fairfax, above n 240.

## *F Addressing the Arguments Against Using Directors' Duties*

### *1 Directors' Duties Already Allow Directors to Take into Account the Interests of Non-shareholder Stakeholders so Change is Not Warranted*

The flexibility in directors' duties that allows them to consider the interests of stakeholders other than shareholders is examined in part VII. It is accepted that this flexibility no doubt allows corporations to make decisions that are in the interests of stakeholders such as the natural environment. What the current law does not do, however, is require directors to do so, which is what this essay proposes. It is argued that an approach similar to that taken in the UK should be adopted in Australia. An equivalent Australian duty would include shareholders, the climate and future generations.

Marshall and Ramsay's research provides evidence of why a change is warranted. In the study, the overwhelming majority of directors, 94.3 per cent, said that their duties were flexible enough to allow them to take into account the interests of groups other than shareholders.<sup>246</sup> However, when ranking stakeholders in order of priority for consideration in decision making, it was shareholders, the company and employees who earned the top spots respectively. Only 2 per cent of directors rated the environment in the top three.<sup>247</sup> This indicates that when directors are merely permitted to consider other interests such as the natural environment, rather than required to, it still tends to be the traditional subjects which get priority. Marshall and Ramsay's results support the call for a duty that raises the profile of the climate and future generations as the only way for these abstract stakeholders to gain the attention of corporate decision makers.

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<sup>246</sup> Shelley Marshall and Ian Ramsay, above n 226, 305-306.

<sup>247</sup> Ibid, 305-306.

## *2 Extending Directors' Duties to a Broader Set of Stakeholders Will Cause Harm by Introducing Uncertainty into the Law*

Any change to the law has the potential to create confusion, and a change to a long-established pillar of corporate law even more so. However, it is not a foregone conclusion and certainly no reason to shy away from law reform that could bring important benefits. Moreover, Marshall and Ramsay's research indicates that confusion around what directors' duties actually require of directors is what exists now, and that change is required to achieve clarity.<sup>248</sup> The new duty proposed in this essay would not only enable corporations to participate in a bottom up approach to climate change mitigation, but also go some way to achieving the clarification Marshall and Ramsay call for.<sup>249</sup>

A new and additional directors' duty is proposed because the current duties are inadequate to deal with the demands of stakeholder theory and intergenerational equity in a climate change context. Currently, directors' duties simply ensure that shareholders' interests are not harmed in instances where other interests are also taken into account. Harm is usually viewed as the loss of assets, rather than any breaches of law that may give rise to penalties or secondary harm such as reputational damage. Purcell and Loftus make the trenchant observation that the current state of affairs can lead to situations where directors make 'rational' decisions to accept penalties for various breaches, where the gains obtained through the breach outweigh the penalty.<sup>250</sup> For example, there may well be circumstances when compliance with environmental legislation would cost more than the penalty imposed for breaching it. Provided reputational damage is not severe, it could be argued that this kind of behaviour is in the best interests of shareholders from a

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<sup>248</sup> Ibid.

<sup>249</sup> Ibid.

<sup>250</sup> John A Purcell and Janice A Loftus, above n 103, 150.

wealth maximisation point of view. While this essay does not purport to suggest that this is ethical or common practice, it does seek to make the point that the proposed directors' duty would circumvent this problem from arising at all because of the impact such a breach would have on future generations and the climate.

One of the strongest arguments against a directors' duty requiring consideration of the interests of a broad group is that it can result in an erosion of accountability. Elaine Sternberg is a strong supporter of this argument, saying that stakeholder theory 'effectively destroys business accountability... because a business that is accountable to all, is actually accountable to none.'<sup>251</sup> Certainly, this is possible, although there is as yet no evidence of this occurring in the UK following its legislative changes. Further, it could be said that the proposed change is really just a codification of what occurs in practice, only with two new, and up to this point overlooked, stakeholders included.<sup>252</sup> Good drafting, clear explanatory notes and the preservation of the good faith element in the new duty will go a long way to avoiding this problem occurring.

Some say that extending directors' duties to accommodate broader stakeholder interests would also introduce uncertainty into the law by imposing potentially conflicting obligations to multiple stakeholder groups.<sup>253</sup> Again, this is possible, but it is argued that a new duty which aims to balance needs, rather than only raise the profile of chosen stakeholders, should not introduce unnecessary uncertainty and conflicting demands. Using the theoretical tools provided by stakeholder theorists such as De Lopez's observations about the importance of primary stakeholders,<sup>254</sup>

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<sup>251</sup> Elaine Sternberg, *Just Business* (Oxford University Press, 2000), 51.

<sup>252</sup> Shelley Marshall and Ian Ramsay, above n 226, 311-312.

<sup>253</sup> John A Purcell and Janice A Loftus, above n 103.

<sup>254</sup> Thanakvaro De Lopez, above n 122.



summarised in part V, will assist directors in deciding how best to balance conflicting demands. Interpretation aids can also play a role. These are used to good effect in the UK legislation, where explanatory notes specifically say that the list of stakeholders provided is not exhaustive and that the aim is to highlight where community values lie in order to assist directors in balancing these interests.

### *3 The Corporations Act is Not the Appropriate Tool For Enhancing Corporate Attention to Social Issues*

A strong argument against using the *Corporations Act* to achieve social or environmental goals is that other, separate legislation designed with that purpose in mind will be better for the job.<sup>255</sup> Turning to the writings of Sealy, we see that this argument has had support for a number of decades. In Sealy's opinion, corporate law 'must acknowledge that it has no mechanism to ensure the fulfilment of obligations of social responsibility.'<sup>256</sup> It is contended that this is not entirely true, and that the history of the corporate form, outlined in part IV, clearly shows how corporations do indeed serve a social function, even if it is still not quite correct to say they owe a social obligation.

Purcell and Loftus also make the point that legislation that aims to regulate the behaviour of all people, not just company directors, is a far superior way of pursuing a social agenda.<sup>257</sup> This point appears to carry particular weight in the climate change context because every individual is an emitter of GHG. In response, this essay suggests that because corporations emit by far the most GHG when compared to

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<sup>255</sup> John A Purcell and Janice A Loftus, above n 103, 147-152; Karen Bubna-Litic, 'Mandatory Corporate Reporting: Does it Really Work?' (2004) *Keeping Good Companies* 615; Andrew Lumsden and Saul Fridman, 'Corporate Social Responsibility: The Case For a Self Regulatory Model' (2007) 25 *Companies and Securities Law Journal* 147.

<sup>256</sup> Len S Sealy, above n 228, 176.

<sup>257</sup> John A Purcell and Janice A Loftus, above n 103, 149.

individuals, they are the logical place to start. In addition, it is also far easier and less expensive to measure and control the emissions of corporations than of individuals or even households.

Others have made arguments against corporate law pursuing social ideals in relation to issues such as equal opportunity, employment relations, community welfare and the ‘traditional’ environmental problems of pollution, contamination and smog, etc.<sup>258</sup> While these issues certainly played out in the corporate arena, they were rightly and effectively addressed by separate legislation. This is because they were *tame* problems. Tame problems, the opposite of wicked problems examined in part II are simple to define; it is possible to fully understand them and, critically, possible to know when they are solved. Thus, discrete and prescriptive legislation is an ideal legal tool for solving these types of problems. As discussed at length in part II, climate change is none of these things. For this reason it is argued that the *Corporations Act*, an Act always designed to balance a complex set of interests while still fostering economic benefit, is indeed the most appropriate tool for the job.

*G Directors’ Duties Possess Many Features That Make Them an Appropriate Tool in a Bottom Up Approach to Climate Change Mitigations*

*1 Established Remedies and Penalties*

One of the most important ways the *Corporations Act* can play a role in a bottom up approach to climate change mitigation is through the use of its existing remedies and penalties that apply when directors fail in their duty to ensure corporate compliance. Introducing a new duty to take into account the interests of future generations and the climate exposes directors to a new set of risks. This provides a more effective

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<sup>258</sup> See eg, Adolf A Berle, above n 78; Milton Friedman, above n 81.

incentive than the repercussions that potentially flow from allowing the corporation to breach its obligations imposed by other legislation. Directors' duties do not operate to ensure that directors conduct the affairs of the company in accordance with the general law, nor do they necessarily make a director liable for a breach by the company of some other provision of the *Corporations Act*.<sup>259</sup> If climate change is accepted to be a problem of unprecedented scale and severity, then an approach that is unapologetic in its imposition of responsibility and penalty is necessary.

This essay proposes an undeniably tough stance, but it is also one that offers directors the most freedom in developing innovative solutions to the problem of GHG emissions. A directors' duty is unique in that it allows corporations to reduce their emissions in a manner that aligns with their unique corporate strategy. In this way, directors maintain their control and their discretion. This is crucial as the management of climate change, we have seen, is not well managed by prescriptive, one-size-fits-all legislation. Directors' duties are a legal tool that offer companies the opportunity to exploit their internal expertise and become a part of a bottom up approach without unfairly hindering their ability to remain competitive and succeed.

## *2 Clearer Obligations Pave the Way for Innovation*

This essay calls for a new approach to climate change mitigation. It advocates a bottom up approach that includes corporations and their directors as key players. It identifies corporate governance that balances the needs of shareholders, the climate and future generations as a way to achieve this. By harnessing directors' duties, the

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<sup>259</sup> *Australian Securities and Investments Commission v Warrenmang Ltd* (2007) 63 ACSR 623; *Australian Securities and Investments Commission v Maxwell* (2006) 59 ACSR 373. However, in some circumstances it can be a breach of the director's duty of care for the director to authorise or permit the company to contravene the *Corporations Act 2001* (Cth): *Australian Securities and Investments Commission v Warrenmang Ltd* (2007) 63 ACSR 623, [25]; *Australian Securities and Investments Commission v Rich* [2009] NSWSC 1229, [7238]; *Australian Securities and Investments Commission v Citofresh International Ltd (No 2)* [2010] FCA 27, [40]–[60].

incentives to innovate, and the ability to remain competitive and increase wealth remain. Put another way, this approach recognises that when left to their own devices, free-market businesses will generally figure out the best, most effective way of doing things within given restrictions. A directors' duty, rather than another form of regulation, offers the flexibility to best allow this to happen. Purcell and Loftus sum up this idea, saying 'if there are highly persuasive pressures that compel sensitivity to the impact of business on external interests, supported by sound business rationale, a degree of proactive involvement by business is likely to generate better regulatory outcomes for itself.'<sup>260</sup> It is difficult to think of an issue exerting more persuasive pressure than climate change.

Imposing a duty on directors allows sound business rationale to underpin any emissions reducing initiatives organisations choose to undertake. There is evidence that adopting a business-sensitive approach will lead to corporate benefit. The 2006 Carbon Disclosure Project Report, commissioned by Goldman Sachs JBWere and the Investor Group on Climate Change Australia and New Zealand, acknowledges that climate change has the potential to impact the earnings of many companies in the medium to long term.<sup>261</sup> The report goes on to note climate change has the potential to adversely impact financial performance and long-term investment value.<sup>262</sup> Crucially, this report finds that while companies are generally aware of the climate change related risks they face, implementation of steps that would limit the negative impact of climate change has been limited. The report found that only 25 per cent of companies demonstrated a sophisticated understanding of the climate change risks associated with their operations. It is suggested that part of the reason for this inaction is that directors feel restrained by their s 180 duty and the common law

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<sup>260</sup> John A Purcell and Janice A Loftus, above n 103, 151.

<sup>261</sup> KPMG Australia, above n 50, 7.

<sup>262</sup> Ibid.

equivalent. The low implementation rate could also be partially explained by the current regime which simply allows companies to pay for their emissions, instead of actively looking for ways to reduce them.

### *3 Minimum Regulation*

The proposed new directors' duty forces corporations to take action within a framework that boasts strong enforcement mechanisms but largely allows corporations to set their own rules. Importantly, it provides corporations a chance to develop innovative solutions to the climate change management problem with minimal rules – the duty need not be part of an onerous compliance regime. Climate change, it has been shown, cannot be effectively managed via prescriptive, regimented rules. A regulatory approach that permits creativity and flexibility and that accommodates rapid change – even if it is clumsy and inelegant – is what is required.

This approach to corporate regulation is generally supported by the business community which is aware that, if they cannot accept responsibility for the consequences of their actions and decisions, then they will 'increasingly be obliged to play by rules that are progressively imposed upon them.'<sup>263</sup> Adopting the proposed directors' duty will permit directors the freedom to harness the creativity and innovative resources within their companies. This in turn allows for decisions that align with each corporation's unique strategy.

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<sup>263</sup> Rick Sarre, 'Responding to Corporate Collapse: Is there a Role for Corporate Social Responsibility?' (2002) 7 *Deakin Law Review* 1, 13.

## *H Drafting the Duty*

This essay does not purport to examine different drafting options for this duty in any detail. Rather, it has sought to identify and highlight the important matters that should be included by the drafting. In so doing, a simple example of what the duty may look like is used, but this not intended to be seen as a firm or final version of the new duty.

The new duty must ensure that the interests of the climate and future generations, as stakeholders important to a company's continued survival, are protected and considered by directors in corporate decision making. Crucially, the duty must not be read as to diminish the importance of shareholders, but instead to balance the needs of these shareholders, future generations and the climate. The element of good faith and a business judgment rule similar to that currently contained in section 180(2) of the *Corporations Act* must be maintained. This is similar to the approach adopted in the UK with the Guidance Note provided with the Companies Bill stating,

[a]ny decision as to what will promote success [of the company], and what constitutes such success, is one for the directors' good faith judgment. This ensures that business decisions on, for example, strategy and tactics are for the directors, and not subject to decision by the courts, subject to good faith.<sup>264</sup>

This guidance illustrates how explanatory memoranda and other interpretation aids can be of use. Such aids including information about the principles of intergenerational equity and stakeholder theory would be developed and included.

The proposed new duty could conceivably read along the following lines:

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<sup>264</sup> Department of Trade and Industry (UK), 'Guidance on Key Clauses to the Companies Bill' (3 November 2005) 17.

In carrying out their duty to act in good faith in the best interests of the company as a whole, directors are required to have regard to, inter alia, the following:

- a) the likely consequences of any decision in the long term; and
- b) the impact of the company's operations on the climate, and future generations' needs to access natural resources.

### *I Establishing Breach*

Although the *Corporations Act* provides for effective enforcement of directors' duties, establishing breach is nevertheless often very difficult. Directors' duties are deliberately not prescriptive. They can't be, because the standard of behaviour they require changes relative to circumstance. It is impossible to articulate precisely what is required of directors in a way that would apply in every situation. This reality has founded one of the main criticisms levelled at the new UK legislation. Andrew Keay identifies that there is no objective assessment of the actions of the directors, and that there are no definite standards against which the actions of directors can be assessed as major flaws in the reformed *Companies Act* and section 172 particularly.<sup>265</sup> He contends that directors can merely claim to have acted in good faith to make their position 'virtually unassailable.'<sup>266</sup> If this is true, then both the UK legislation and the duty proposed in this essay would suffer the very same enforcement issues that current climate change instruments do.

In response to this argument, this essay argues that 'bright line tests' of managerial behaviour, that is, specific, rigid and detailed standards against which to measure impugned behaviour are not useful in controlling corporate behaviour. Such tests

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<sup>265</sup> Andrew Keay, 'Tackling the Issue of the Corporate Objective: An Analysis of the United Kingdom's 'Enlightened Shareholder Value Approach'' (2007) 29 *Sydney Law Review* 577.

<sup>266</sup> *Ibid*, 586.

would be impracticable in trying to determine whether a director's behaviour and decision making was reasonable in the circumstances. Section 180(1) of the *Corporations Act* already reflects this reality by including a test that is couched in vagueness and relative terms. There is a good reason for doing so – imposing a 'bright line test' will only allow for a solution to be engineered around it.

In any case, there is judicial commentary for guidance on how behaviour in regards to this duty might be assessed. In *Re HIH Insurance Ltd; Australian Securities and Investments Commission v Adler*<sup>267</sup> Santow J was of the view that in determining whether a director has exercised reasonable care and diligence, one must ask what an ordinary person, with the knowledge and experience of the defendant, might be expected to have done in the circumstances.<sup>268</sup> *Daniels v Anderson*<sup>269</sup> made it clear that there are minimum standards of behaviour expected.

Thus, two important points can be made. The first is that it is indeed possible to measure and assess behaviour in line with duties that do not set out prescriptive tests, but rather a general standard. Secondly, courts have shown themselves to be adept at making such assessments, and drawing conclusions about whether or not a breach has occurred. The proposed new duty would therefore be enforceable by traditional means.

### *J Enforcing the New Duty*

#### *1 Who Will Have Standing?*

For the new duty to be effective in mitigating climate change, it must make directors accountable to the very stakeholders whose interests are to be taken into account.

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<sup>267</sup> (2002) 168 FLR 253.

<sup>268</sup> (2002) 168 FLR 253, 372.

<sup>269</sup> (1995) 37 NSWLR 438.



That is, the climate and future generations. The obvious problem with this is that neither can bring an action themselves, and so questions arise about who may have standing to do so on their behalf. This is a critical question as lack of enforceability has been identified time and again as a reason for the failure of the current climate change mitigation regimes.<sup>270</sup> This is especially so in light of the evidence from the UK that section 172 of the *Companies Act* may end up being a toothless tiger.<sup>271</sup>

While it is recognised that these issues of standing and enforceability are crucial to the success of the new duty proposed here, this essay does not attempt to design in any detail the mechanisms by which it will be administered. This essay has sought primarily to argue the case for directors' duties to be utilised as part of a bottom up approach to climate change. The intricacies of how this new duty will be monitored and enforced are identified as the subject of further research. Nevertheless, this section provides some brief comments on possible enforcement structures.

It is likely that a specialist body with standing to bring an action on behalf of these stakeholders will need to be established. Brown Weiss suggested an ombudsman-like body<sup>272</sup> and Christopher Stone speaks of 'guardians' who would represent the natural environment in the present and in the future.<sup>273</sup> These concepts could easily accommodate future generations and the climate as stakeholders in need of representation. Stone suggests some functions this body could serve. They include monitoring compliance, intervening in disputes, recommending changes where necessary and having standing in legal proceedings.<sup>274</sup>

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<sup>270</sup> See, eg, Prins et al, above n 1; Prins and Rayner, above n 1.

<sup>271</sup> Keay, above n 240; Keay, above n 266.

<sup>272</sup> Edith Brown Weiss, above n 149, 10-12.

<sup>273</sup> Christopher D Stone, 'Defending the Global Commons' in Phillippe Sands (ed) *Greening International Law* (Earthscan, 1993) 34.

<sup>274</sup> *Ibid.*

The *Corporations Act* already contains several mechanisms for enforcing directors' duties. Shareholders can bring an action against company directors where they believe the directors have acted in breach of their duties.<sup>275</sup> This new duty would retain this shareholder right, but it is conceded that this rarely, if ever, happens and would be even less likely in the context of a breach of the proposed duty. It is proposed that shareholders should not be able to ratify a breach of this duty, as they currently can in regards to some breaches.<sup>276</sup> The Australian Securities and Investments Commission (ASIC) also has the ability to bring an action for the breach of certain duties so it could potentially take up the monitoring of this new duty as well.<sup>277</sup>

The final point to be made here is that there is growing support for specialised judges and courts in the environmental crimes and litigation arena.<sup>278</sup> The establishment of any new body, or the granting of additional powers to an existing body, would need to examine the case for a specialised court and judicial officers.

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<sup>275</sup> *Corporations Act 2001* (Cth) s 199A.

<sup>276</sup> A company in general meeting may ratify a director's breach of fiduciary duty, provided there has been full disclosure: *Winthrop Investments Ltd v Winns Ltd* [1975] 2 NSWLR 666. Breaches of statutory duties, however, cannot be ratified by members: *Corporations Act 2001* (Cth) s 199A.

<sup>277</sup> *Corporations Act 2001* (Cth) ss 1317E(1) and 1317J(1).

<sup>278</sup> See, eg, Reece Walters and Diane Solomon Westerhuis, 'Green Crime and the Role of Environmental Courts' (2013) 59(3) *Crime, Law and Social Change* 279; Rob White, 'Environmental Crime and Problem Solving Courts' (2013) 59(3) *Crime, Law and Social Change* 267; Jacqueline Peel and Michael Power, 'Climate Change Law: Lessons From the Californian Experience' (2010) 27 *Environmental and Planning Law Journal* 169.

## X CONCLUSION

In sum, it has been shown corporations have real potential to play a critical role in a new, bottom up approach to effective climate change mitigation. Up until now corporations and their directors have been all but ignored in the climate change debate. An over reliance on environmental law principles and climate change instruments based on other instruments used to address entirely different types of problems have led to ineffective climate change mitigation policy. The rise of non-state actors as legitimate participants in global issues, stakeholder theory and intergenerational equity combine to form a sturdy argument for imposing on company directors a duty to take into account the interests of the climate and future generations as well as shareholders.

Stakeholder theory and intergenerational equity work to inform the proposed new duty. Stakeholder theory acknowledges that corporations depend on the climate for their survival, and shows that the climate is capable of having an enormous impact on corporations' success. Intergenerational equity ensures that present and future generations are not deprived of their rights to access the Earth's natural resources. A directors' duty to take into account the climate, future generations and shareholders will ensure that corporate decision making can better balance the interests of these stakeholders in a way that leads to effective climate change mitigation. The current law is too unsettled to permit this to happen; directors face uncertainty around the extent to which they may consider the interest of stakeholders other than shareholders. For corporations to be a part of a bottom up approach to effective climate change mitigation it is necessary to establish a new duty which specifically imposes on directors an obligation to take into account the interests of shareholders, the climate and future generations

Directors' duties have been identified as an ideal legal tool for including corporations in climate change mitigation efforts because they are widely acceptance and well understood. Critically, their enforcement mechanisms are also accepted and well understood. This means the proposed duty will avoid the significant problem of lack of enforceability facing the current international and domestic instruments, and other voluntary corporate social responsibility measures aimed at mitigating climate change. Importantly, the new duty would include a business judgment rule defence similar to that in existence now in order to protect directors acting reasonably and in good faith.

This new approach to climate change mitigation harnesses the immense power held by corporations and their directors. It aims to develop an approach that balances the needs of shareholders, the climate and future generations in a manner that does not sacrifice the benefits of incorporation. It is very important that climate change is addressed and mitigated. It is equally important that corporations are able to aggressively pursue profit goals. Directors have shown themselves adept at operating under onerous duties that ensure shareholders are rewarded and at the same time social values are protected. In a similar way, the adverse impacts of climate change present a social problem worthy of legal attention. A directors' duty to take into account the interests of shareholders, the climate and future generations has the potential to form part of the first effective approach to climate change mitigation.

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