Journal of the British Academy

Volume 10, Supplementary issue 5
2022

Foundations of the Future of the Corporation programme report 'Policy & Practice for Purposeful Business'

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ISSN 2052-7217

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Journal of the British Academy, **10(s5)**, 1–15
https://doi.org/10.5871/jba/0010s5.001
Posted 26 August 2022

The research background to the final report of the Future of the Corporation programme on '*Policy & Practice for Purposeful Business*'

Colin Mayer

Abstract: This article introduces four research papers that were written for the final report of the British Academy Future of the Corporation programme. It focuses on three areas – corporate law, measurement, and finance. The overarching concept that the programme has developed is of corporate purpose being about creating profitable solutions to problems of people and planet, not profiting from producing problems for either. Adoption and implementation of this requires corporate law to reflect the extension of the boundaries of the firm beyond their conventional ones of property ownership and contractual claims to include the impact that the firm has on others. That should be incorporated in measurement systems that determine the success and profit of a company and in particular account for the costs of rectifying and remedying detriments that it inflicts on others. The purpose of financial systems and institutions in this context is to ensure that the necessary financial resources and forms of investor engagement are available to allow firms to deliver on their purposes. Finally, several cases studies illustrate the extent to which companies are implementing meaningful purposes and the challenges they face in doing so.

Keywords: Corporate purpose, law, measurement, finance.

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Objective

In November 2018, the British Academy produced its first report on the Future of the Corporation, entitled *Reforming Business for the 21st Century*. The report set out what looked at the time to be an ambitious programme of reform of business around its corporate purpose. It suggested a move away from the conventional notion of corporate purpose as being about furthering the interest of shareholders to one that recognised the role of business in addressing the challenges we face as individuals, societies and the natural world in the 21st century.

It emphasised the need for business to address these challenges in a form that is commercially viable, profitable and financially sustainable, while avoiding profiting from causing detriments to other parties. It therefore argued that the purpose of business is 'to produce profitable solutions for the problems of people and planet, not profiting from creating problems for either'.

Since the first report was published, there has been a substantial global recognition of the ideas presented in the British Academy report and, in November 2019, the British Academy produced a second report entitled *Principles for Purposeful Business*. This report described four pairs of principles to promote the reform of business around its purpose. The principles relate to:

- Law and regulation
- Ownership and governance
- Measurement and performance
- Finance and investment

In the final 2021 report entitled *Policy & Practice for Purposeful Business*, the programme developed the principles into several specific policy proposals. The task it set itself was to answer the question: if the proposition that the purpose of business is or should be to 'produce profitable solutions for the problems of people and planet, not profiting from creating problems for either', what should then follow from this as the required policy and practice reforms under the eight principles?

There are good reasons for using this notion of purpose as a starting point. It takes the desired purpose of business as being to do things we want it to do and not profit from doing things we don't want it to do. It is not about promoting the interests of stakeholders over shareholders or the adoption of corporate purposes in a general aspirational sense. It is about the specific objective of solving not creating problems.

That seems compelling but the question is can it be achieved in a credible form? Can we identify a set of policies categorised in the eight areas that would give logical coherence to the emergence of corporate purposes which solve problems profitably and assist business with achieving this?

To illustrate, we start with the current concept of the purpose of a firm as being to promote the success of the business for the benefit of its shareholders. Underpinning this is a set of eight policies that provide a logical framework for this notion of 'shareholder primacy':

- *company law* establishes the fiduciary duties of directors to be to promote the success of the company for the benefit of its shareholders;
- *regulation* determines 'the rules of the game' within which companies operate, and the enforcement of these rules;
- *ownership* is about the rights of shareholders;
- *corporate governance* seeks to resolve 'the agency problem' between shareholders and management and align management interests with those of their shareholders;
- *measurement* is about accounting for financial and material assets and liabilities;
- *performance* is evaluated in relation to corporate profits;
- *finance* promotes the benefits of investors; and
- *investment* is about maximising shareholder value.

The important point is that all policies are consistently and coherently structured around shareholder interests and therefore reinforce each other in achieving it. The attainment of a new purpose of business around profitable solutions of problems will require an equally consistent and coherent set of policies. We suggest that the following offer as compelling a framework for this new set of policies to achieve a system change:

Company law

Company law will need to be framed around a company's purpose. There is much discussion about whether existing law is sufficiently permissive for companies to adopt purposes beyond shareholder interests, therefore making it unnecessary to change the law. That debate, we would suggest, misses the point.

A company purpose is the reason why a company exists and is created, and it should therefore logically lie at the heart of laws that establish it. Companies should define why they exist and justify the immense privileges that are conferred on them through their perpetual existence and limited liability. In particular, they should establish what benefits they confer on others in return for those privileges and affirm that the benefits that they themselves derive from their profits are not earned at the expense of others. The law should require firms to demonstrate that their constitutions – their ownership, governance, measurement and performance – ensure the fulfilment of their purposes.

Regulation

Regulation performs two functions. First, it determines the detriments from which companies should not profit and should rectify where they arise. It should establish the minimum conditions that companies must fulfil in deriving a profit, and the expenditures they must incur in remedying detriments and compensating others for the damage they have caused.

Most companies should be free to determine their corporate purposes, conditional on not profiting from producing detriments for others. Indeed, a multiplicity of corporate purposes should be encouraged to promote entrepreneurialism and innovation in business. This enhances competition and the functioning of markets, and it encourages 'runs to the top' in competing to produce profitable solutions to problems.

However, there is a class of companies whose purposes need to be specified by virtue of the activities they undertake and the sectors of the economy in which they operate. These are sometimes described as 'regulated firms', in particular utilities, financial institutions, auditing companies and some public service providers. The second function of regulation is to ensure that the purposes of these companies are consistent with their 'social licences to operate'.

Ownership

To give meaning and effect to a company's purpose, someone has to own and take responsibility for it. Ownership in this context naturally relates to why the company exists and its reason for being. It is not ownership of the property of the company or its assets but ownership of what the company is there to do. The company may have no assets, or at least no measurable tangible assets, but it still has a significant reason for being for which someone or a group of people need to take ownership.

When a company is established, the founder defines and promotes its purpose. Where founders pass on and sell their shares in substantial blocks to members of their families, private equity investors or other companies, then these parties become the natural owners. More generally, shareholders who provide the financial risk bearing capital should have a real sense of ownership and commitment to the company's purpose.

Where shares are widely dispersed on stock markets then the board of directors of companies and the executives have particular responsibility for the company's purpose. The executive and the board should be guided by the purpose as the determinant of the firm's strategy and culture, and the basis on which resources are allocated and performance measured throughout the organisation.

However, ownership of a corporate purpose should not reside just at the top of an organisation. Ownership is a collective endeavour between all those involved in the delivery of a purpose. Those parties should feel inspired and motivated to contribute as best they can to its realisation. Successful leadership involves giving everyone within an organisation a real sense of ownership of their part of the company purpose. It is determined by consultation throughout the organisation and realised through adoption by every part of it.

Corporate governance

Corporate governance establishes the basis on which a company's board and executive directors are appointed, held to account and remunerated. The board and the executive are responsible for the determination of the firm's strategy to deliver its purpose, the required resources, the culture and values of the company, and the company's system of measurement performance, incentives, and rewards.

Beyond the board itself and its committees, shareholders have a defining role in the appointment, accountability, and remuneration of members of the board. That process should be determined by the nature of the company's purpose and the people and resources required in its delivery. Shareholders, as providers of finance and bearers of financial risk, have an important role to play in this, but so too might other parties, in particular employees.

The formulation and determination of a company's strategy in fulfilment of its purpose should involve those who are most significant in its delivery. The corporation of the future will use citizens assemblies, social media, big data, and other innovative techniques to encourage their participation and engagement.

Measurement

Measurement relates to the activities of the firm regarding its inputs, outputs, outcomes, and impacts. It establishes qualitative and quantitative metrics of the resources required in fulfilment of the firm's purpose, the changes it brings about as a consequence of its purpose, and the impact it has on the well-being of others.

Performance

Performance is measured in relation to fulfilment of the company purpose of solving problems profitably, while avoiding and rectifying any detriments it causes. It is reflected in the way in which it costs the resources it employs, determines its profits, and measures the benefits and detriments it confers on its customers, societies, environment, and investors.

Financing

Financing should ensure that the company is adequately resourced in terms of the scale, form and duration of funding it requires to deliver its purpose. A company should determine its financial policy – dividend distributions and capital structure – in such a way as to ensure that it has sufficient resources and resilience to sustain its purpose and avoid imposing detriments on others in the future.

Investment

Investment should be undertaken at the scale, places and times needed to a deliver a company's purpose. Companies should invest in their customers, employees, suppliers, communities, societies, nations, nature and the environment in partnership with other organisations in the commercial, charitable and public sector in fulfilling the purposes they have in common.

In sum, a coherent, consistent set of policies for purposeful business takes the following form:

- *company law* requires directors of companies to determine their purposes and associated constitutions;
- *regulation* determines minimum acceptable standards and alignment of purposes of regulated firms with their social licences;
- *ownership* of corporate purposes is the responsibility of holders of blocks of shares, boards of directors, executives and employees;
- *corporate governance* requires the participation and engagement of those parties most relevant to the successful delivery of companies' purposes;
- *measurement* is required of the inputs, outputs, outcomes and impacts of companies' purposes;
- *performance* accounts for the costs, profits and values of the outcomes and impacts of companies' purposes;
- *finance* ensures that companies have the scale, type and duration of funding required to resource their purposes; and
- *investment* is undertaken at scale, places, and times in partnership with other parties to fulfil their common purposes.
- This involves implementation of reforms to:
- company law and regulation are the particular remit of governments and regulators;
- ownership and governance of investors and firms;
- measurement and performance of standard setters and accounting bodies; and
- finance and investment of financial institutions, firms, not-for-profit and public sector organisations.

This comprehensive policy framework can then be used to identify specific reforms that are required in different contexts. The final report of the Future of the Corporation programme takes the UK as a country to illustrate this for several reasons. The first is that the UK is in many respects at an extreme in terms of its adoption of shareholder primacy. Its legal, regulatory, ownership, governance, measurement, performance, financial and investment systems have all been very coherently structured around an exceptionally dispersed ownership of company shares. It is therefore a country where the challenges of reform in adopting other purposes are particularly great.

Second, the UK is a country that has been used as a model internationally for the adoption of its 'common law' legal form, privatisation and regulation of its utilities, minority investor protection, corporate governance codes, accounting standards, and its financial system. Reform of the UK system could therefore be particularly influential at a global level.

Third, the adverse impacts of the shareholder primacy model on social and regional inequality, poor productivity, and underinvestment by the corporate sector have been very pronounced in the UK. The potential benefits of reform may therefore be especially significant in the UK. References to the UK should be regarded as an illustration of the way in which the policy framework set out in the report can be adopted universally to provide a comprehensive basis for reform of business in any country around the world.

Methodology

The Future of the Corporation programme produced 17 academic papers involving more than 40 researchers, it engaged over 200 experts in 29 deliberative, evidence-generating roundtables and 100 stakeholders in eight 'Purpose Labs' over a period of four years between 2017 and 2021. Four research papers were commissioned on law, measurement, finance, and case studies of companies incorporating purposeful objectives in their businesses. The policy labs were organised on corporate law in conjunction with the law firm, Bates Wells; on regulation with the think-tank, Sustainability First; on governance with the Cambridge Institute for Sustainability Leadership; on measurement and disclosure with the UK Financial Reporting Council; and on climate finance with the Bank of England.

This issue of the *Journal of the British Academy* brings together a report on the policy labs, and the four commissioned papers. The first article, 'Findings of the Future of the Corporation "Purpose Labs"' by Jocelyn Bailey, Lilian Barratt, Molly Morgan Jones and Henry Richards (2022), summarises the policy labs. It describes a total of 42 specific policy reforms that were considered across the labs and how they culminated in an assessment of the ‘urgency’ and ‘feasibility’ of each reform. The result is a striking assessment of how urgency and feasibility are often aligned, but by no means always.

For example, wholesale reforms to embed purpose in the heart of corporate law, to achieve international collaboration on regulation and standard setting of corporate activities and corporate reporting, or to effect changes in corporate taxation that promote corporate purposes are difficult to achieve. But there is a great deal that might be done in the interim to promote corporate purpose in terms of encouraging companies to take advantage of provisions that exist within current legal statutes, and to use other tools such as corporate governance codes and government procurement to bring about change. In other words, there is much that can be achieved to promote corporate purpose in the short run while more comprehensive reform is pursued over a longer period.

Corporate law

In ‘The Future of the Corporation: the avenues for legal change’, Dalia Palombo (2022) sets out a cogent discussion of how law should be formulated to promote both a ‘Purpose Objective’ and a ‘Do No Harm Objective’. Palombo states that ‘the Purpose Objective should re-connect directors, shareholders and stakeholders in order to ensure that businesses rediscover their original function to serve the needs of society.’ ‘The Do No Harm Objective should ensure that businesses are accountable when they damage the stakeholders affected by their activities.’

Palombo contrasts two types of legal instruments that are available to promote these two objectives: ‘control’ and ‘accountability’. Control relates to rights of approval and removal of board members, and derivative actions and oppression remedies against directors on behalf of companies and affected parties respectively. Accountability relates to the power to hold companies to account for the detriments they inflict on others, including potentially extraterritorially in their supply chains. Extending control rights from shareholders to include stakeholders would promote a Purpose Objective and making firms accountable to their stakeholders as well as shareholders through tort law or regulation would give effect to a Do No Harm Objective.

However, a delivery of a stakeholder agenda comes at the expense of a considerable extension to governance and accountability, sounding the alarm that ‘accountability to everybody is accountability to nobody’. The problem reflects a conflation of accountability and responsibility. Quite deliberately, the Future of the Corporation programme definition of corporate responsibility does not include a ‘do no harm objective'. It is a do not profit from doing harm objective. Companies do harm all the time in closing factories, laying off people, and building roads and houses in the countryside. But in doing so they should incur the costs of remedying, rectifying, mitigating, or compensating the detriments they cause and make provisions when they are anticipated. Where this is not financially viable then they should desist from the detrimental activities.

The significance of this is that 'producing profitable solutions for the problems of people and planet, not profiting from creating problems for either' is therefore not just a statement about solving problems but also about defining profit and determining what is a legitimate source of profits. Profits that are earned at the expense of others without remedying, rectifying, mitigating, or compensating detriments are not legitimate. They are only legitimately earned where problems are solved not created. If profits fulfil this criterion, then, by definition, all profitable activities enhance wellbeing as well as the wealth of investors.

Companies can therefore remain solely accountable to shareholders and still be assured of promoting social wellbeing provided that the costs that companies incur reflect those of remedying, rectifying, mitigating, and compensating the detriments they cause and desisting from activities where this is not the case. This obligation stems from recognising that companies are responsible for the interests of all parties on whom they impact and depend, not just those they supply and employ. They are responsible for establishing where problems arise, how they are best addressed and whether they are profiting from creating them. This involves them in engaging and consulting with parties on which they impact and depend, and evaluating the detriments caused and the costs of addressing them. Aggrieved parties have redress through the courts and torts, and in cases where there is a public interest or potential for monopoly abuse through regulation and public law.

The effect of the above is to extend the boundaries of the firm beyond their legally contractual inputs and outputs to their consequential outcomes and impacts. This internalises the costs of remedying detriments that are external to the contractual liabilities of firms. Companies are required to incur and anticipate these costs, and account and provide for them as appropriate. Nothing else changes and the formal accountability of firms to their shareholders proceeds as before. However, a great deal changes substantively because by restricting profit and value creation to problem solving not problem causing, the focus of the firm shifts to identifying innovative ways of creating commercially viable solutions to problems of individuals, societies, and the natural world. In other words, companies are automatically incentivised to do what we want of them, not what we wish they would not do.

Measurement

In 'Through the looking glass: tying performance and materiality to corporate purpose', Judith Stroehle, Kazbi Soonawalla and Marcel Metzner (2022) describe how the concepts of single and double materiality that have come to dominate the corporate reporting world relate to corporate purpose. Single materiality refers to the impact of society and the natural world on its financial performance. Double materiality relates to the impact of the firm on society and the natural world, i.e., a reverse causation from single materiality. So, for example, climate change might affect the performance of a firm – single materiality – or the firm might contribute to climate change – double materiality.

As Stroehle et al argue, from the point of view of a purpose of a firm being 'to produce profitable solutions to the problems of people and planet', single materiality is relevant to the profitability of the solutions and double materiality is relevant to whether the firm is solving the problems of people and planet. So corporate purpose as defined by the Future of the Corporation programme demonstrates elements of both single and double materiality.

However, there is more to it than that because there is a second part to the definition of a corporate purpose and that is that the company 'should not profit from producing problems for either people or planet'. This relates to single materiality in not profiting from detriments and to double materiality in the determination of detriments that companies might cause. Furthermore, combining the two halves of the definition, if firms only profit from producing solutions not from creating detriments, then there is a direct association of profiting in a single material sense from benefiting people and planet in a double material sense. Furthermore, the causation is from the latter to the former. In other words, there should only be positive single materiality (i.e., financial gain) where there is non-negative double materiality (i.e., an absence of societal and natural world detriments). Where there are detriments there should not be profits.

What this does is to establish the notion of a legitimate profit as arising only if there is no societal or environmental detriment. Otherwise, companies are profiting at the expense of others in engaging in wealth transfer rather than wealth creation. The direction of causation therefore runs from solutions to profit because problems must be corrected before profits are earned.

The way in which this happens is that companies mitigate, rectify, remedy, or compensate detriments before they declare a profit, and accounting for profit incorporates the costs of so doing. That way profits reflect the full or true costs of companies in making amends and cleaning up the mess of the problems they create irrespective of whether they are associated with the contractual liabilities of the firm. In other words, what the definition of the purpose of the company does is to extend its boundaries beyond what it owns and what it does to what it causes and who it affects.

The power of this is that once one recognises what a true profit of a firm is then there is a direct relation between that and the promotion of societal and natural world benefits. Profits are only earned where there are benefits not detriments. It is no longer, and it should not be, an empirical question of whether there is a positive relation between the impact of firm on the world in which it operates and its profitability. It is a matter of definition that profits are only earned where there are benefits without detriments.

It is this that is ultimately the resolution of the deficiencies of our system of capitalism as currently constituted. We have, predominantly over the past sixty years, but progressively since freedom of incorporation swept the world in the 19th century, suffered from a growing disconnect of the financial – the primacy of individual financial gain – from the communal – the connectedness of the individual to the community – and the ecological – our relation to the natural world. Together they are incredibly powerful ways of promoting advancement through combining the material with the emotional, our needs with a sense of belonging, and what is desired with what inspires. Where they pull in different directions they cause individual mental distress, social distrust, and physical disasters.

The redefining of corporate purpose is therefore not only significant in terms of defining the objective of the firm but also the determination of what is a legitimate profit. It establishes the costs companies incur in both avoiding profiting at the expense of others – expropriation – and delivering solutions for their benefit – creation. Not only does this therefore establish a way of avoiding the current misalignment between private incentives and public and planetary interests, but it also provides a very practical tool for managing corporations in such a way as to promote the delivery of commercially viable solutions. It determines the basis on which those working in organisations can track their contribution to the corporate purpose, the boards of companies can evaluate the success of the firm in delivering their stated purposes, and investors can engage with companies in determining the allocation of financial resources to the achievement of their purposes.

Finance

Key to the fulfilment of businesses purpose is the financial sector. As David Pitt-Watson and Hari Mann (2022) describe in 'The purposeful corporation and the role of the finance industry', there are four key functions that the financial sector performs: it provides safe-keeping of financial assets, a payment system, risk sharing through insurance and investment institutions, and financial intermediation between savers and borrowers.

Regarding the promotion of corporate purpose, the last two functions are particularly important. The financing of corporate purpose requires financial institutions to provide finance in the form and duration that companies need to resource their purposes. Risk sharing equity funding is particularly significant in that regard and, for start-ups, scale-ups, and small and medium sized enterprises (SMEs), this is often difficult to obtain at the scale that is required, particularly for those operating in regions of countries that are disconnected from their financial centres.

The financing of firms raises complex issues of relationships between borrowers and savers. The delivery of purposes of solving problems requires the provision of finance on a duration and scale that involves long-term relationships between firms and their investors. Bank finance is particularly important in the early stages of development of firms. However, this often takes the form of working capital not the term-lending, or even more significantly long-term partnerships between banks and SMEs which are found in some countries, such as Germany, but absent from many others, including the UK.

The problem that the financial sector raises is one of trust. Contracts alone are a weak and inadequate basis on which to build long-term relations. Strong relationships involve a close physical proximity and personalised engagement between lenders and borrowers that forge strong bonds of trust between them. These require people with skills and knowledge that extend beyond lending, portfolio, and fund management to a real understanding of the nature and running of businesses.

Financial intermediation is based on advising, mentoring, networking, and nurturing the growth and development of businesses as well as such traditional functions as credit scoring, investment appraisals and investment analyses. Those skills are in particularly short supply in developing countries and regions of countries that are distant from their financial centres. In the absence of such intermediation skills, investors and firms remain at arms-length from each other, trust between the two is weak, costs of capital are high, and funding constraints are widespread.

But the problem is even more serious than that. Shareholders are not only providers of finance they are also the holders of shares in companies which confer voting rights as well as financial benefits on them. They have rights of approval and removal of directors of companies and sometimes rights of approval over their remuneration as well. That makes the boards of companies accountable and beholden to their shareholders. Without the support of their shareholders, even the most enlightened directors cannot implement their corporate purposes.

The resolution of this issue has focused on two approaches. The first is communication and the second is measurement. Directors of companies need to communicate effectively with their investors about their purposes and demonstrate not only their social and environmental benefits but also the financial returns they yield for investors. That is why corporate purposes of necessity must provide profitable solutions. A critical part of that communication is financial reporting and the provision of quantitative measures as well as qualitative evidence on the success of the company in delivering on its purpose.

Communication, measurement, and engagement by institutional investors in dialogue with boards about corporate purposes are critically important but not sufficient. Investors can signal their strong support for management's stated purposes at one moment but then, faced with a hostile acquiror or a hedge fund activist offering a higher price for their shares, withdraw their support at the next. That is why so many financial systems around the world have a variety of impediments to what is termed 'the market for corporate control' in the form of dual class shares, anti-takeover devices such as poison pills, and dominant holders of blocks of shares.

All these reveal fundamental defects of existing arrangements to promote corporate purposes in the absence of legal systems that explicitly recognise the centrality of purpose. Unless the fiduciary duties of directors of financial institutions as well as non-financial corporations are to promote purposes of 'producing profitable solutions for problems of people and planet, not profiting from producing problems for either', then neither will be able to deliver them. That is why, as Pitt-Watson and Mann argue persuasively in their article, the purpose of finance is as important as the purpose of corporations, and both depend on each other for their success.

Examples

The final article in this issue, 'Principles of purposeful business: illustrative examples' by Charles Ebert and Victoria Hurth (2022), reflects this very clearly. It sets out how many companies over the last few years have embraced the notion of corporate purpose. They have done so for a variety of reasons because they recognise it as simply good business to promote the interests of customers, employees, environment, societies, and suppliers. It creates more loyal customers, more engaged employees, more reliable suppliers and more supportive environments and societies. They believe it is 'the right thing' to do and that, although it might be costly in the short-run, in the long-run it creates more robust, resilient, socially acceptable businesses that are less at risk from financial failure and regulatory interventions.

The cases presented in the article report companies at different stages on what they frequently refer to as 'a journey' of discovery and implementation of corporate purpose. The process of determining, defining, simplifying, and communicating it takes time. Implementing and connecting it with the corporate strategy, values, and culture, and measuring and reporting it take much longer. Adoption of corporate purpose is not therefore by any means straightforward.

While the companies in the study are to be commended for what they seek to do, the cases reveal a varied level of progress and a limited scale, breadth, and depth of adoption to date. Some companies are relatively small, others only incorporate their purposes in certain parts of their businesses, few provide compelling evidence of their effects on the parties with whom they engage or the financial benefits they confer on their investors, and none explicitly refer to solving problems, not profiting from producing them.

While not wishing to denigrate in any way what has been achieved to date, the concern is that current legal, measurement and financial arrangements limit the extent and speed of progress that companies can make. So long as this remains the case, there is a risk that corporate purpose will go the way of its predecessor, corporate social responsibility (CSR), and be perceived as a passing fad of no significant long-term consequence. That would be very damaging. It is inconceivable that the reason why business exists, is created, its reason for being, namely its purpose, can be anything other than of profound significance for business and the world around it. To the extent that this is not understood or accepted then there is a failure to appreciate what a corporate purpose of profitably solving not creating problems for people and planet means for customers, employees, the environment, nature, shareholders, societies, and suppliers.

Conclusion

The question that was posed at the beginning of this article was, can the objective of establishing corporate purposes of producing profitable solutions for problems of people and planet be credibly delivered? The articles featured in this issue were just one part of the large body of research, evidence, expertise, knowledge, and opinion that were collected to answer this question. Nevertheless, they point clearly to answering it in the affirmative. We can develop systems of corporate law, accountability, measurement, and finance that are as coherent at producing problem solving as their predecessors were at producing profit maximisation.

The great advantage of the former over the latter is that it ensures that business and finance do what we wish of them, namely, to enhance social wellbeing and prosperity for all. However much we might believe in the efficiency of markets, the power of contracts, and the adequacy of regulation, our experience of the last sixty years has revealed their limitations. Profits have been earned at a serious cost to global prosperity at the same time as markets, contracts and regulation have proliferated. Solving this involves a systems transformation that places profitable solutions rather than profit maximisation at the heart of law, measurement, and finance of companies and financial institutions.

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To cite the article: Mayer, C. (2022), ‘The research background to the final report of the Future of the Corporation programme on “*Policy & Practice for Purposeful Business*”’, *Journal of the British Academy*, 10(s5): 1–15.
https://doi.org/10.5871/jba/010s5.001

Journal of the British Academy (ISSN 2052–7217) is published by
The British Academy, 10–11 Carlton House Terrace, London, SW1Y 5AH
www.thebritishacademy.ac.uk

Journal of the British Academy, **10(s5)**, 17–41
https://doi.org/10.5871/jba/0010s5.017
Posted 26 August 2022

Findings of the Future of the Corporation 'Purpose Labs'

Jocelyn Bailey, Lilian Barratt, Molly Morgan Jones and Henry Richards

Abstract: This article presents the findings of the Future of the Corporation 'Purpose Labs' that took place between September and December 2020. It is a synthesis of the outputs and notes captured by the authors who facilitated the sessions and the proposals referenced are described for context rather than as an evaluation or recommendation. The labs themselves brought together stakeholders of the Future of the Corporation programme – policy and business experts, thought-leaders, and stakeholders interested in the application of corporate purpose to the business ecosystem – alongside several expert partner organisations. They used the *Principles for Purposeful Business* (2019) as a starting point and a range of methods to engage participants in developing insights into current policy and practice, as well as emerging or new ideas and proposals. They were followed by a process of analysis and review, which then fed into the concluding report of the Future of the Corporation programme.

Keywords: Future, corporation, purposeful, business, policy, system, law, governance, measurement, finance.

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Introduction

The British Academy, the UK's national academy for the humanities and social sciences, launched the Future of the Corporation programme in 2017.[1] The programme quickly established itself as one of the leading platforms for debate on the changing role and nature of business in the 21st century. Using the British Academy's convening power to bring together leading practitioners from around the world on business and finance, civil society leaders representing all walks of life, academics from a wide range of disciplines, and of course, policymakers, the programme provided new opportunities for debate across some traditional divides. This article is concerned with its final phase and the development of a final set of proposals; however, the programme has been iterative with each phase and element building on the last, so before proceeding, we have reviewed the first two phases.

The programme started with the broad question, 'What is the role of business in society?' Its first phase of research, a landscape review produced in 2018, highlighted some of the reasons why this question matters now: the global nature of challenges that society faces and the global nature of business itself; the opportunities and challenges presented by new technology; the increasingly intangible nature of companies; and, the perceptions of business in wider society that undermine trust. This 2018 research also demonstrated the importance of corporate purpose as a means to align interests of all stakeholders in the business around a single objective – an answer to the question, 'Why does this company exist?' Finally, this first phase used engagement with academics and practitioners to explore some of the levers of change for business practice and policy, looking at the role of owners and ownership, corporate governance frameworks, regulation, corporate taxation, and investment. The core conclusion of this first phase was that business practice and policy need to focus on trustworthiness, ethical cultures, and above all a sense of purpose. Bringing together the research, a new definition of corporate purpose was set out in our 2018 report, *Reforming Business for the 21st Century*: 'The purpose of the corporation is to produce profitable solutions for the problems of people and planet … not to profit from producing problems for people and planet.'

The second phase of the programme started with this definition and set out to elaborate on its meaning. The process involved four evidence generation and synthesis components: convening of a Deliberation Group; commissioning of evidence syntheses (Palombo 2022; Pitt-Watson & Mann 2022; Stroehle *et al.* 2022); generating new ideas and insights through a series of deliberative roundtables; and a final analysis

[1] The Future of the Corporation programme research is available at https://www.thebritishacademy.ac.uk/programmes/future-of-the-corporation/research

to generate the principles supported by review and consultation with participants in the process. The final output of this was a generalised description of the nature of *purposeful business* through eight general principles that promote it. These are:

1. *corporate law* should place purpose at the heart of the corporation and require directors to state their purposes and demonstrate commitment to them;
2. *regulation* should expect particularly high duties of engagement, loyalty and care on the part of directors of companies to public interests where they perform important public functions;
3. *ownership* should recognise obligations of shareholders and engage them in supporting corporate purposes as well as in their rights to derive financial benefit;
4. *corporate governance* should align managerial interests with companies' purposes and establish accountability to a range of stakeholders through appropriate board structures; they should determine a set of values necessary to deliver purpose, embedded in their company culture;
5. *measurement* should recognise impacts and investment by companies in their workers, societies and natural assets both within and outside the firm;
6. *performance* should be measured against fulfilment of corporate purposes and profits measured net of the costs of achieving them;
7. *corporate financing* should be of a form and duration that allows companies to fund more engaged and long-term investment in their purposes;
8. *corporate investment* should be made in partnership with private, public and not-for-profit organisations that contribute towards the fulfilment of corporate purposes.

By setting out these principles, the programme gives meaning to a notion of purposeful business that is focused on solving the problems of people and planet using financially sustainable and commercially viable models, while not profiting from creating problems. Our 2019 report, *Principles for Purposeful Business*, argued that a purposeful business will organise itself on all levels according to its purpose, but that these principles specifically do not *prescribe* those purposes and do not encourage others to prescribe them. Rather, they describe the features of the operating environment that enables the delivery of those purposes, while remaining flexible to a diversity of business models, cultures and jurisdictions.

The third phase of the programme set out to explore the practical implications of the principles, through contrasting approaches. While the *Principles for Purposeful Business* are not specific to a single country or jurisdiction and draw on insight from around the world, the final phase considered the application of the principles specifically to the UK. The process in this third phase combined a series of high-profile

Purpose Summits involving business leaders, investors, civil society leaders, politicians, regulators and academics in public discussions on policy and practice, with a series of 'Purpose Labs' about which this article is concerned. A third, smaller element explored examples of practice which are available in this issue (Ebert & Hurth 2022).

After the methodology section below, this article is presented in three main sections. The first sets out the initial set of proposals derived from the first round of Purpose Labs sessions convening stakeholders with insight into the themes. This was, in essence, a brainstorming exercise and did not involve filtering or evaluation of the proposals. The second section reflects the output of the second round of labs sessions in which the proposals were discussed with a broader group according to the principles they related to – law & regulation, ownership & governance, measurement & performance, and finance & investment. It summarises some of the context around the discussions and then presents the details of proposals discussed in the Purpose Labs. The third section provides a visual representation of the findings of a survey conducted during the labs to collect views on the feasibility and importance of all the proposals described in the first section. This survey helped to identify areas of consensus around the proposals.

Methodology

Over recent years there has been a proliferation of practices and initiatives, both in the UK and globally, aimed at bringing evidence closer to policymaking, at 'opening up' policymaking to input from a more diverse range of sources and voices, and at introducing collaborative, creative and generative methods into policymaking practice. 'Policy Lab' is a term often associated with this trend, although in practice a broad range of activities and entities are gathered under its banner: from workshops and events, to teams or organisations, or even a physical space. At the British Academy, we use the term Policy Lab to mean an iterative process engaging academics, experts and practitioners in small groups to generate new thinking and insight into the application of policy principles arising from SHAPE research. In this section we set out the approach and methods we used in delivering the Future of the Corporation 'Purpose Labs', which combined research and insight into the nature of the challenge, multiple and diverse perspectives and voices, and design-based methods for creative collaboration and generating practical policy proposals.

Round 1

The first five Purpose Labs were held in September and October 2020 in partnership with several organisations helping to develop best practice on key elements of the purposeful business framework. They brought together around six to eight practitioners and experts, including the Financial Reporting Council (FRC),[2] the Cambridge Institute for Sustainability Leadership,[3] environmental think tank Sustainability First[4] and law firm Bates Wells.[5] Each lab session, organised virtually due to the pandemic rules, was organised around a central question/s, designed to identify and develop practical suggestions around each theme:

- How do you report on purpose? How do you make meaningful reporting for purpose-based companies?
- How can governance be aligned with delivering purpose-driven organisations? What does 'good' look like and how do we ensure we get there?
- What can regulators do to create the best environment for companies to deliver on purpose (understood as social, environmental and economic outcomes)?
- How should 'purpose' be enshrined in law? If Section 172 is going to change to reflect a requirement for directors to promote 'purpose', how should it change?
- How can we mainstream the climate agenda so it is taken into consideration in all investment/ financial decisions?

For each session, a bespoke agenda was designed, incorporating a mix of discussion and co-design activities. A write up of the key insights and proposals was produced for each workshop, circulated to the group of facilitators, and a final synthesis workshop brought this core group together to assess what had emerged. Taken together, the first round of workshops produced a long list of 43 practical proposals, reproduced below in Section 1.

Round 2

In November 2020, three identical (in terms of format) sessions were held, in order to further explore, add detail to, as well as critically analyse and evaluate the 43 proposals. To do this, an activity template was devised which took small groups of participants through answering a series of questions, in relation to each proposal (Figure 1). The 43 proposals were divided up over the three workshops, in which participants were

[2] https://www.frc.org.uk/
[3] https://www.cisl.cam.ac.uk/
[4] https://www.sustainabilityfirst.org.uk/
[5] https://bateswells.co.uk/

Instructions: read me first

- Nominate someone to act as scribe and someone to chair/ lead the group through the questions
- There are 4 brainstorming activities
- Read the proposal in the black box and then discuss the questions in the pink boxes, following the numbering
- Write answers and comments in the white boxes.
- Spend about 5 minutes on each box - try to move fairly quickly: perfection is not the goal!

The basic proposal 01

A major review into the mandate and powers of economic and business regulators with particular attention to purpose, participation and accountability, and a principles-based approach.

1. Framing/ situating the proposal

- What kind of proposal is this - policy or practice? Where should the emphasis fall?
- Is this an end point or a stepping stone? If an end point, do we need to define intermediate steps?
- Are there any critical interdependencies with other changes?

It is principally a policy proposal.

It also concerns the mandates and practices of regulators.

However, a prior concept of what purpose looks like in a practical context when applied by business is needed.

As a review, it is a stepping stone and an intermediate step. It might apply to a number of regulators.

Arguably, all economic and business regulators are already thinking about wider stakeholders and no review is therefore needed and no review would be additive.

It may therefore boil down to what concept of purpose is informing any such review and whether it is needed. There may be deficiencies in the current system of regulation .

2. Getting practical

- How could this be taken forward? What would it look like in reality?
- Who are the key responsible actors? What should they do?
- Who else is implicated and what should they do?
- What resources or inputs are required?
- What would a rough project timeline look like?

- A request to Government to undertake a broad-based review of business and economic regulators mandates.

- The key actors would be regulators and other stakeholders interested in their activities.
- Corporates, directors of corporates, consumers, and a very wide group of stakeholders
- It would involve official time and associated research costs.
- There would be a need to compare different regulators mandates and spotting gaps.
- 6-12 months for a review and report. A few years for any legislation.

3. Moving forward

- How could you test (and improve) this proposal in a low-risk way?
- Where would you start? What would you do first/ tomorrow?

- It might be possible to conduct some initial research independently of a Government backed review.
- It might be possible to scope such a review and the kinds of issues it would present, such as disclosure, governance, product design and other considerations within individual markets.
- It might be possible to look at areas of market failure – examining the outcomes in certain markets, where these are deficient – and reverse engineering how it might be possible to address these issues in the underlying economic and business
- It would be possible to survey and interview regulators about their own mandates to understand where they might feel bound or limited.

4. Ambition and impact

- What does success look like in the short, medium and long term? What is the ideal end point?
- How will we know if it's working?
- Why should time and resource be spent on this?

- Looking at the regulatory system as a whole might be a way of seeking to reduce the negative externalities created across the economy. At the moment, different regulators would have a different view on the relevance and responsibility for negative externalities.

Figure 1. Example of activity template from Round 2.

divided into groups of around five to critically assess two proposals in depth. They were asked to address questions about the actors responsible for the proposal, whether it relied on any interdependencies, what a timeline would look like and what the next steps would be.

Using a survey tool, we then asked participants to rank all of the proposals on a scale of 1 (low) – 5 (high) in terms of their feasibility and their importance / urgency. This helped us to create a rough overview of how the proposals could be prioritised. Using the survey scores we mapped the proposals across a 2×2 matrix of urgency vs feasibility (see Section 3 below).

Following these Round 2 sessions, a synthesis of the discussions and the outputs of the completed activity templates was produced. This formed the basis for the conclusion of the process which entailed a series of iterative dialogues with stakeholders in the Future of the Corporation programme to assemble and refine the proposals to be included in programme's final report, which was published as *Policy & Practice for Purposeful Business* in September 2021.

Section 1: initial proposals

The first round of the Purpose Labs, as described above (Round 1), took the 2019 *Principles for Purposeful Business* as an input and asked how those principles could be applied in practice. The principles are universal in nature and so need interpretation based on the legal and regulatory environment, the business culture, political economy, and other relevant context. The exercise produced a rich set of inputs that reflected the varied make-up of the participants in these discussions. These inputs were then the basis for the second round of discussions.

Readers should be aware that the list does not represent a consensus view or the view of the British Academy and we do not describe or evaluate the proposals here. They are included to illustrate the starting points for the discussions synthesised in Section 2 and as a reference for the 2×2 grid reproduced in Section 3, where the numbering below matches the labelling on the chart.

1. A major review into the mandate and powers of economic and business regulators with particular attention to purpose, participation and accountability, and a principles-based approach.
2. A major review of business taxes and other government support to correct for any possibility of 'profiting from creating problems' and encourage purposeful business.
3. Announcement of reform of Section 172 of 2006 Companies Act, initiating a major consultation process.
4. BEIS (the UK Government's Department for Business, Energy and Industrial Strategy) to produce optional guidance and model articles of association for purpose driven companies.
5. Changes made to the explanatory guidance to s172(2), some guidance from BEIS developed to encourage people to use the existing legislation in a new way to embed purpose.
6. Setting the mandate of ARGA to give life to the purpose agenda with powers to hold companies to account for bad behaviour.
7. Give new regulatory oversight powers to Companies House to investigate and act upon breaches of new corporate governance requirements to give them teeth.
8. Public procurement and government behaviour need to set an example. The UK government has set ambitious climate targets, yet this is not reflected in their own purchasing practices.
9. Government should consider policies to enable blockholdings (holding of significant proportions of company shares).
10. All boards must set the framework that enables a company and its stakeholders to enact its purpose.

11. All board members should be motivated to serve all their stakeholders, including the environment. Boards committed to a corporate purpose will be able to use this as a framework for making decisions.
12. There needs to be clear relationships between boards and management teams with empathy and understanding all the way down the chain.
13. The relationship between boards and employees should be strengthened through encouraging greater representation both by employees at board, and through board members interacting more with management and the wider workforce.
14. All boards should establish a moral and ethical framework connected to purpose that is operative within the organisation.
15. Enable senior executives by creating the right decision-making frameworks. There is a need for integrated frameworks for decision-making so that ESG (Environmental, Social and Governance) related key performance indicators aren't in conflict with all the other targets.
16. Business leaders should build an understanding of the challenges around a stakeholder approach and seeking out new data, knowledge and skills to support change.
17. When it comes to investing, we need to think at system level not just portfolio, and move from ESG to impact.
18. Any proposals for widespread reform need to be based on evidence and so more analysis of the performance of purpose led companies like B Corps (companies committing to the 'B Corp' standard on purposeful business) are needed, so that everyone can have confidence that a more purpose-led economy as a whole will work.
19. Employee ownership should be championed as a method of achieving high levels of engagement, responsibility and commitment to social purpose.
20. Fiduciary duties for employees: should there be a provision in the Companies Act that codifies the fiduciary duties of employees to include promoting the purpose of the company?
21. Should employee representation on boards be mandated? Though there is no legal obstacle to it at present, it very rarely happens.
22. Development of model articles for a specific legal form for profit-with-purpose business, so that businesses have the option to incorporate or convert to this form. Model articles could set out how the shareholders have agreed to mandate the directors to balance and integrate other stakeholder interests more deeply.
23. Require firms to adopt 'positive purposes' into Articles, as described in s172(2).
24. General requirement for boards to 'integrate' ESG factors into strategy (moving beyond the requirement to 'have regard to' stakeholder interests).

25. There is a need for an external enforcement of corporate governance because s172 is very rarely subject to litigation and there needs to be external monitoring of compliance with any new enhanced corporate governance requirements.
26. Financial reporting alone is no longer sufficient. One integrated report should be produced with purpose directly linked to business outcomes as well as non-financial impacts, which can be used to engage and inform all of a company's stakeholders and not just shareholders.
27. Over time, it will be necessary to move to a single impact reporting standard. An interim requirement on boards of firms above a certain size to choose and adopt a comprehensive impact reporting and assessment system (e.g. GRI, SASB, B Impact Assessment) perhaps ratified by the shareholders, which sits alongside current accounting and reporting requirements.
28. There is a need to develop accurate measures for externalised impacts and costs, which might be quite varied depending on the sector. We need to expand the range of non-financial indicators and develop ways of sharing performance on more qualitative social factors (the 'S' in ESG).
29. Supporting development of international disclosure standards to yield decision-useful, comparable and aggregable data, and coalescence around measurement methodologies and assumptions used for forward looking metrics, for example Impact Management Project, ISO standards, IFRS.
30. Other stakeholder voices are important in the reporting process. The workforce has an important role to play in terms of critiquing or supporting claims around purpose, but there is a need for a collective mechanism for staff to input in a way that doesn't put individuals at risk.
31. Financial institutions could be mandated to publish their plans for climate alignment, focusing on supporting the overall transition to a green economy – moving away from regulation on disclosure of risk to regulation of impact.
32. Regulators should move towards a tiered set of standards that involve the regulator setting out a strategic vision for the sector, which aligns with the government's strategic policy statement for the sector, with outcomes that companies should ultimately be able to deliver.
33. A new regulatory model should be focused on outcomes or principles-based regulation (rather than prescriptive or rules-based), where the regulator would determine a set of required outcomes but leave space for companies to innovate. Principles need to be developed in discussion between key stakeholders (policy, regulatory, company and wider civil society groups).
34. Price reviews in monopolies would need to be more clearly aligned with a longer-term strategy – i.e. a broader 'price path'. Companies need to feel that they are empowered and have the space for those conversations with stakeholders

about how to put purpose into practice, beyond short-term economic constructs and models.

35. Regulators could set targets for institutional investors for the rate at which they decarbonise their portfolios alongside financial returns.
36. There is a need for professionalization of directorship and director's training. At present many directors, particularly at smaller firms, have little grasp of their existing duties and require more developed support mechanisms.
37. Professional training or qualifications for asset managers and financial advisors on purposeful investment
38. There is a need for greater expertise on boards with regard to stakeholders beyond shareholders and directors need to take into account a broader base of information in decision-making. Develop toolkits for understanding who are your stakeholders and how to engage them.
39. Citizen Assemblies and other deliberative stakeholder engagement mechanisms can be a useful tool in allowing people to hear and understand the trade-offs that companies face and can be a channel to provide meaningful input and help develop a more consensual approach. How can they be mainstreamed as an engagement tool?
40. Develop toolkits and responses to challenging 'trade-off' issues which counter 'zero-sum' narratives and help people find better solutions to difficult decisions.
41. Developing frameworks for assessing performance which are broad enough to capture different contributions to purpose – financial incentives may not be appropriate.
42. Integration of *Principles for Purposeful Business* into business teaching at universities.
43. Educating and mobilising of consumers to demand green financial products. For example, we need green options for where pensions are invested.

Section 2: proposals by principle

The proposals generated in the first round of labs sessions were then organised by the conveners around the eight *Principles for Purposeful Business* and presented in the second round of labs sessions. In these sessions, they were considered as a whole as well as in regard to the principle they relate to and some proposals were presented under multiple principles. Below, we explore in more depth those proposals which had the most interest from participants organising them around the *Principles for Purposeful Business*. We introduce some context and details of how the proposal might be applied based on the discussions and we note whether there was any existing practice or policy to build on.

A. Law and regulation

The proposals in this section refer to two *Principles for Purposeful Business*.

- **Corporate law** should place purpose at the heart of the corporation and require directors to state their purposes and demonstrate commitment to them.
- **Regulation** should expect particularly high duties of engagement, loyalty and care on the part of directors of companies to public interests where they perform important public functions.

The Purpose Labs discussions focused primarily on corporate law in terms of the laws governing the way business operates and regulation as the regulations applying to business and the regulators themselves. Here we reflect the discussions and key points made around each proposal.

Proposal: BEIS (the UK Government's Department for Business Energy and Industrial Strategy) should publish optional guidance and model articles for a specific legal form for profit-with-purpose business

Publicising official but optional model articles for profit-with-purpose business, such as B Corps, would give businesses the option to incorporate or convert to this form. It would also help to ensure that alternative forms of purpose are seen as official, legitimate and safe. Detailed case studies should be developed to raise awareness of the benefits and performance of purpose driven businesses and to encourage a race to the top.

The argument made for this in the labs was that model articles could set out how shareholders have agreed to mandate the directors to balance and integrate other stakeholder interests more deeply.

Proposal: The explanatory guidance to s172(2) of the 2006 Companies Act, should be updated to encourage businesses to use the existing legislation to embed purpose

The traditional view, brought out in the labs, is that this sub-section is designed for use by charities and not by commercial organisations, who by default comply only with s172(1). The guidance should be used to encourage businesses, in the short term, to use this existing piece of legislation to embed purpose and to serve their wider stakeholders.

The FRC (Financial Reporting Council) has produced detailed guidance on embedding and reporting on purpose. The s172(2) explanatory guidance would benefit directors by offering shorter key requirements. It could usefully require companies to give practical examples of how they are fulfilling their purpose through core business activities rather than separate CSR style exercises.

As participants explained, implementing this legal mechanism at a company level would require buy-in from senior stakeholders including directors and shareholders. This approach would also impact company reporting, in that it would necessitate accountability to all the firm's stakeholders (see Measurement and Performance below).

Proposal: Reform Section 172 of 2006 Companies Act, requiring firms to adopt 'positive purposes' into Articles

The discussion explored the problem with the current arrangements. While the success of the company continues to be interpreted purely in financial terms, meaningful consideration of stakeholder interests will remain secondary to the duty of directors to benefit a company's members. Considering this from another angle, the law currently does not *prohibit* the prioritisation of returns to shareholders, even when they come at a cost to the company's wider stakeholders. For both reasons, an amendment and strengthening of the language of the Companies Act will be necessary to make the duty of a director to promote the purpose of the company, and operate the company in a manner that benefits its members, wider society, and the environment. Possible wording for such an amendment is demonstrated in The Better Business Act Coalition's proposed amendments to Section 172 of The Companies Act 2006.[6]

Beyond this argument, participants also made the case that Section 172(1) sets the standard and default approach for companies in the UK economy and therefore needs changing to reflect a move to focus on purpose. But any change should be made in a way that facilitates companies having options where appropriate and is not unduly prescriptive. A company must benefit wider society and the environment in a manner commensurate with its size and the nature of its operations.

Such a change would require a major consultation and analysis would be needed of how companies articulate purpose currently, building on that currently being conducted by the FRC's analysis of reporting against the Corporate Governance Code. Companies would need to be given adequate time to adapt, and to formulate and implement their purposes.

This proposal, as discussed, would entail legislation that eventually required all companies to articulate their purpose in their articles of association and to report on how it benefits wider society and the environment, the harms it creates or costs it imposes on wider society and the environment and, separately, the actions it is taking to reduce or eliminate those harms and costs. Requirements would need to be consistent across ownership types but adjusted for company scale.

[6] https://betterbusinessact.org/wp-content/uploads/2021/04/The-Better-Business-Act-2021.pdf and https://betterbusinessact.org/about-the-act/

Proposal: A new regulatory model should be focused on outcomes or principles-based regulation where the regulator determines a set of required outcomes but leaves space for companies to innovate

This would allow flexibility for companies and markets going through dynamic and complex change. It would enable a broader set of positive outcomes than the current model, which tends to be focused on short-term economic efficiency and price rather than wider public interests.

Participants highlighted that looking at the regulatory system as a whole is crucial to reducing the negative externalities created across the economy. The discussion highlighted that agreement would be needed on what the desired outcomes are across different sectors and how they would be implemented through a combination of voluntary standards and mandated outcomes on social and environmental issues.

A regulatory system focused on purpose, would also have a focus on balancing the needs of current and future societal interests, with regulators (and companies) taking a long-term view to protect future generations and address other externalities. Companies need to feel that they are empowered and have the space for conversations with stakeholders about how to put purpose into practice, beyond short-term economic constructs and models. Price reviews in monopolies would need to be more clearly aligned with a longer-term strategy – i.e. a broader 'price path'.

Regulators would need to support companies to engage stakeholders in driving innovation and better outcomes for people and planet. However, participants noted that the principles-based model is reliant on regulators' capacity to have strong relationships with firms based on trust and shared social goals.

Proposal: Regulators should move towards a tiered set of standards that involve the regulator setting out a strategic vision for the sector, which aligns with the government's strategic policy statement for the sector, with outcomes that companies should ultimately be able to deliver.

The discussions highlighted that regulation needs to take a stratified approach for companies at different stages and scales, and according to their performance. A strategy of 'earned autonomy' could be adopted for the best performers, but regulators must still retain the authority to intervene when there is a risk of real harm being done to current and future public value.

For new entrants or poor performers, a two-pronged approach was discussed:

- firstly, ensuring compliance with a minimum set of standards; the regulator would provide clear expectations which are future-focused, providing clarity about what that minimum level will look like over coming years;

- a long-term conversation about strategy that moves the cultural focus beyond short- to medium-term compliance to what the behaviours of a sector-leading company may look like.

For more ambitious or larger firms, there could be stretch objectives, which also provide an idea of what is expected as companies grow. Participants described how this would act as more of a supervisory relationship – particularly relevant for areas where regulators want to stretch company performance. This approach relies on strong relationships between regulators and firms, and particularly developed relationships are needed for large and monopoly companies.

It was noted that regulators may need new skill sets and insights to be able to operate in a more dynamic and participatory environment and to effectively develop a more stratified approach.

Proposal: Regulation should move towards a more democratic and participatory approach, with regulators acting as a conduit for, and enabler of, greater engagement between companies and their stakeholders

This proposal would entail companies embracing new processes of stakeholder engagement while the role of the regulator would be to support and provide guidance in doing so. The discussion highlighted that companies should not only be held to account by stakeholders, but also listen to and learn from them.

Citizen Assemblies and other deliberative stakeholder engagement mechanisms were put forward as useful tools in allowing people to hear and understand the trade-offs that companies face and can be a channel to provide meaningful input and help develop a more consensual approach. This approach allows stakeholders to understand that there are sometimes inherent conflicts in the way that companies (in particular utilities) have to operate. It would ensure that trade-offs and implications are more fully disclosed and debated.

The discussion made it clear that participatory processes only work well if they are fully invested in. It is important that companies close the feedback loop to show that they have listened and how they have come to a decision. If regulators do not pay due regard to company stakeholder engagement processes, and the recommendations flowing from these, they would need to clearly explain the reasons for their decisions. If a trade-off falls harshly on a community, the company in question should acknowledge this and show what it has done to take the issue into account in future or provide a remedy.

B. Ownership and governance

The proposals in this section refer to two of the *Principles for Purposeful Business*.

- **Ownership** should recognise obligations of shareholders and engage them in supporting corporate purposes as well as in their rights to derive financial benefit.
- **Corporate governance** should align managerial interests with companies' purposes and establish accountability to a range of stakeholders through appropriate board structures. They should determine a set of values necessary to deliver purpose, embedded in their company culture.

The Purpose Labs discussions focused more on the corporate governance principle where more concrete proposals were made in the first round discussions. Corporate governance is also an area with significant interest and debate in business and policy circles. Here we reflect the discussions and key points made around each proposal.

Proposal: Champion and expand employee ownership as a method of achieving high levels of engagement, responsibility and commitment to social purpose
Participants briefly discussed this proposal and the need for a more systematic review of existing evidence pertaining to the benefits of employee ownership.

Proposal: Boards should set a framework that enables a company and its stakeholders to enact its purpose through its values, culture and strategy
Future of the Corporation outputs have highlighted that purpose should drive both company culture and strategy. Once purpose is established, the board needs to clearly prioritise decisions in relation to purpose in order to operationalise it. The Enacting Purpose Initiative's 'SCORE' framework outlines clear mechanisms for boards to articulate and implement purpose within their organisations.[7]

The lab session explored the idea that boards may establish a moral and ethical framework connected to purpose that is operative within the organisation. The values of an organisation must be modelled by the board and management team. Participants described storytelling techniques that can be used successfully to communicate values and purpose, for example, after a large merger or acquisition. Managers throughout the company would be involved in this process and purpose narratives can also be built into induction processes. Purpose needs to be integrated into all levels of an organisation with mechanisms in place for employees to feed back up to the board. A range of structures may be needed to support corporate purpose implementation

[7] Enacting Purpose Initiative (2020).

throughout the organisation including codes, compliance regimes and whistle-blower protections.

In addition, the discussion highlighted that boards should empower senior executives by creating integrated frameworks for decision-making so that a company's purpose is clearly reflected in its key performance indicators and not in conflict with financial targets. Project decision-making frameworks could also include external impacts in addition to core value impacts.

Proposal: There is also a need for more developed frameworks for assessing employee performance through different contributions to corporate purpose that do not solely depend on financial incentives

The brief discussion on this proposal picked up on the current problems with financial reward schemes that are a product of a system that values profit maximisation above contributions to other purpose-related goals. Instead, participants noted that companies could identify other non-financial motivators and examine criteria for promotion and how they can be linked more strongly to purpose.

Proposal: Board members should be motivated and equipped with the guidance to identify, engage and serve all their stakeholders

Boards, with the support of shareholders, need to determine who the company's key stakeholders are and the parameters, priorities and procedures for resolving frictions between their interests. Labs discussions highlighted the need for greater expertise on boards with regard to stakeholders beyond shareholders and for directors to take into account a broader base of information in decision-making.

Alternative corporate forms, such as the French *enterprise à mission*, social enterprise and B Corps have accountability to all their stakeholders enshrined in their models. Publicising case studies with details around the process of identifying and engaging stakeholders could help to counter perceived challenges. In addition, international standard setting bodies such as the ISO are working towards the publication of governance standards to help companies define their stakeholders and achieve their purpose over the long term.[8]

Once stakeholder groups are identified, the discussions highlighted the importance of boards building relationships and collaboratively agreeing specific deliverables. The needs of different stakeholders can be represented at board level in a number of ways. One method for this could be non-executive directors with responsibilities for different stakeholder groups. Another mechanism is board committees with specific

[8] International Standards Organisation (ISO) (2021)

duties. However, participants note that this carries a risk of taking decision making power away from the board as a whole, for example with sustainability committees. The AGM might be used as a forum to engage the company's stakeholders.

The relationship between boards and employees needs to be continuously strengthened. Effective employee engagement can inform better decisions, align behaviours and share responsibility. Participants highlighted employees in particular as needing to be empowered to challenge decisions being made at board level. As a critical stakeholder group, the employee perspective needs to be reflected and incorporated into managerial discussions and help define company direction.

Ensuring specific board representation for environmental issues can be challenging. Some companies do this by having environmental NGOs join some board discussions, others have advisory committees. Citizens assemblies and other deliberative stakeholder engagement mechanisms can be a useful tool for collecting and understanding the views of wider society. They can allow people to hear and understand the trade-offs that companies face and can be a channel to provide meaningful input.

New research and guidance is needed to develop toolkits and responses to challenging trade-off issues which help management find better solutions to difficult decisions, guided primarily by the company's purpose. In addition, the labs discussed the need for professionalisation of directorship. New training and more developed guidance around necessary skillsets for boards are crucial as directors' roles continue to change with transformational risks around the environment, technology and health.

C. Measurement and performance

The proposals in this section refer to two of the *Principles for Purposeful Business*.

- **Measurement** should recognise impacts and investment by companies in their workers, societies and natural assets both within and outside the firm.
- **Performance** should be measured against fulfilment of corporate purposes and profits measured net of the costs of achieving them.

The Purpose Labs discussions on these principles also extended to reporting which relates closely to questions of measurement and performance. It also considered both the standards and the methodologies that might be used to collect data. Here we reflect the discussions and key points made around each proposal.

Proposal: Integrated reporting should directly link purpose to financial, as well as social, environmental and other external impacts, with the full spectrum of a company's stakeholders involved in the process

Company reporting needs to be structured around the company's purpose, linking it to the business plan, strategy and key performance indicators, as set out in the Financial Reporting Council's strategic report requirement. Participants highlighted that purpose needs to be defined and articulated as a long-term constant and the reason a company exists.

The Enacting Purpose Initiative proposes a three-stage framework for measuring impact and performance against purpose. The first stage is to set out corporate motives, as expressed through stated purpose, mission, vision and values. The second step is to identify the business metrics that are required to enact purpose, including inputs, outputs, outcomes and impacts. The third is the comprehensive monetisation of these metrics through new methodologies like *enterprise cost-based accounting* or *societal valuation-based approaches*.

Labs discussions noted that financial reporting could enable consideration of how the board has allocated capital to deliver on its purpose through investment by companies in their workers, societies and natural assets both within and outside the firm. Non-financial reporting metrics for externalised impacts and costs are being developed by a plethora of national and international organisations, and global standards will be necessary to encourage companies to compete on performance against these indicators. Participants discussed a particular need to expand the range of non-financial indicators and develop ways of sharing performance on more qualitative social factors relating to employees and wider communities affected by firms.

Proposal: Over time, it will be necessary to move to an agreed set of international disclosure standards, as proposed by the IFRS Foundation, with flexibility based on metrics most relevant to the industry a company operates in

Standards can help people identify what is important, drive good behaviour, embed practices and norms in the business, and counteract 'green-washing' by helping stakeholders outside the company understand and make judgments. However, discussions emphasised the risk that over-standardisation would turn reporting into a 'box-ticking' exercise, with less emphasis on the individual company. There is great variation between companies in terms of the salient risks and opportunities (e.g. extractors need to think about land rights, apparel companies about workers' rights). Therefore, standardisation needs to be balanced with a recognition of company individuality.

There is a need for a clear methodology for impact reporting which is consistent, allows comparison between companies, is practical and that auditors can audit against. One suggestion was for an interim requirement on boards of firms above a certain size to choose and adopt a comprehensive impact reporting and assessment system such as *GRI*, *SASB*, *B Impact Assessment*, ratified by the shareholders, which sits alongside current accounting and reporting requirements. More details on measurement systems can be found in Stroehle *et al.* (2022).

Proposal: Reporting should be relevant to and reflective of the interests and concerns of a company's stakeholders

The Enacting Purpose Initiative in its Measuring Purpose – an Integrated Framework paper specifies four main audiences for reporting on purpose, though other groups such as employees, customers and civil society may also be relevant:

> The first is the executives of companies who formulate strategies, allocate resources, and incentivize people in their organizations on the back of measures of performance. The second is middle management who make investment decisions, implement projects and deliver performance within their organizations. The third is institutional investors who make portfolio allocations, monitor investments and steward the companies in which they invest. The fourth is policy makers who seek to align corporate behaviour with public interest and promote public investments, frequently in partnership with the private sector. A system of measurement must serve the needs of at least these four parties if business and economies are to operate effectively.[9]

Labs participants spoke about the important role the workforce has to play in terms of critiquing or supporting claims around purpose, but there is a need for a collective mechanism for staff to input in a way that does not put individuals at risk. Many workplaces have recognised trade unions, which constitute an important and established conduit for collective engagement and more could be done to involve them in the reporting process, which could include employee satisfaction and turnover rates. Discussions highlighted the importance of supporting unions in sectors where they are less well-established as a verified worker voice with the authority to speak confidently to management.

Changes taking place to practice were discussed, driven by the new Corporate Governance Code requirements which has seen many companies begin to report on employee engagement in their Section 172 reports. However, only a fraction are currently reporting on the long-term impacts on stakeholders.

[9] Barby *et al.* (2021: 1).

D. Finance and investment

The proposals in this section refer to two of the *Principles for Purposeful Business*.

- **Corporate financing** should be of a form and duration that allows companies to fund more engaged and long-term investment in their purposes.
- **Corporate investment** should be made in partnership with private, public and not-for-profit organisations that contribute towards the fulfilment of corporate purposes.

The Purpose Labs discussions on these principles considered the type of funding available to purposeful businesses as well as some of the legal and regulatory measures that affect that and the relationship between public and private sector funding. Here we reflect the discussions and key points made around each proposal.

Proposal: Institutional investors should be accountable to interests of their beneficiaries and for the system level impacts of their portfolios

Like the Corporate Governance Code, the UK Stewardship Code is voluntary and not reflected in the law, which currently limits the discretion of trustees in broadening their duty from maximising returns to members to take account of social and environmental factors. Although pension trustees have to publish a stewardship policy as part of their Statement of Investment Principles, commitment to stewardship varies greatly and labs discussions considered how new legal requirements could be introduced as part of a fiduciary investors' duty.

ShareAction's proposal for a Responsible Investment Bill[10] seeks to address this issue. It stipulates that fiduciary investors, particularly pension fund trustees, must act for the benefit of the beneficiaries as a whole. It stresses fairness between the beneficiaries, including as between present and future beneficiaries. It proposes that they have regard (amongst other matters) to:

(a) the likely consequences of any investment activities in the long term;
(b) the impact of any investment activities on the financial system, the economy, communities and the environment;
(c) environmental, social and governance considerations (including, but not limited to, climate change) which the fiduciary investor considers financially material; and
(d) the views of beneficiaries.

This legal proposal embeds double materiality – that is the notion that companies report both on matters of financial and non-financial materiality. It requires investors

[10] ShareAction (2020).

to factor in the risks of social and environmental issues on the value of their investments in addition to the impact their investment decisions have on society and the environment, through measurement and disclosure standards. Transparent, accessible and reliable data are key for beneficiaries to understand how institutional investors are performing against social and environmental measures. The ShareAction bill also states that fiduciary investors have a duty to base their stewardship and investment decisions on the views of their beneficiaries and to communicate how they have done so.

In addition, the Investor Forum and the Pensions and Lifetime Savings Association have developed a framework for institutional investors to deliver effective stewardship and engagement through setting expectations of asset managers and in monitoring and appraising the activities of managers, in order to deliver the best results for beneficiaries and wider stakeholders.[11]

Proposal: Regulators could set targets for institutional investors for the rate at which they decarbonise their portfolios and mandate them to publish plans for climate alignment

Labs discussions on this proposal highlighted the need for further examination of how financial regulation can focus on supporting the overall transition to a sustainable economy – moving away from regulation on disclosure of risk to regulation of impact.

Proposal: New professional training for asset managers and financial advisors on how to factor environmental and social factors into their investment decisions

Participants highlighted the problem that many financial advisors and asset managers lack competence and confidence which it comes to social and environmental impacts and many investment institutions prefer to stick with familiar approaches. Managers need to be equipped with new skills and tools and be motivated to take in a broader base of information when making decisions.

An example of an institutional investor seeking to broaden its skillset can be found in the joint initiative between AllianceBernstein and Columbia University's Earth Institute, which began in 2019.[12] This saw the asset manager send its investment staff, chief executive and board of directors, to the university to learn about how climate risks should be factored into their investment decisions.

[11] See Pensions and Lifetime Savings Association & The Investor Forum (2020).

[12] See https://www.alliancebernstein.com/corporate/en/corporate-responsibility/environmental-stewardship/columbia-partnership.html

Despite this example, participants made clear the need for a more uniform and mainstream approach, which may ultimately require compulsory professional qualifications and reforms to university curricula.

Proposal: Public procurement should encourage and give advantage to purpose-driven companies

The scale of Government spending each year on buying goods and services from external suppliers was noted in the labs. This highlights the potential for government to play a role as a *customer* with substantial power to influence the behaviour of companies bidding for public contracts.[13] Participants also spoke about efforts to strengthen the Social Value Act so that companies are scored with a 10 per cent weighting on the value they provide to society, alongside value for money.

Another initiative discussed was the British Standards Institute's BS 95009 standard on public sector procurement aims to reduce barriers for smaller and more innovative businesses in winning public contracts and helps ensure that contracts are awarded to companies that provide products or services in the best way, without compromising ethics, quality or value for money.[14]

Section 3: overview of feasibility and urgency

Towards the end of each Purpose Lab session, participants were invited to read a sub-set of the proposals and give a score in a survey on two factors: the feasibility and urgency of the proposal. The intention was to provide a secondary point of reference to accompany the discussions and facilitate the analysis following the Labs of how suitable each proposal was. It was not a vote, but rather a rapid evaluation and the conclusions were taken alongside the discussions and context during the analysis and synthesis process. Participants were also invited to feedback on the emerging analysis which was presented in a session convened after the draft analysis was ready. In the grid shown in Figure 2, the numbers each refer to a proposal that is listed in Section 1 of this article (the full text of each proposal cannot be placed in the grid for space reasons). The position of the label horizontally illustrates the average urgency score given by participants from low to high, left to right. The position of the label vertically illustrates the average feasibility score given by participants from low to high, bottom to top. This presentation was not intended to be taken in isolation or treated as a full

[13] Ong & Goyder (2019).

[14] See https://www.bsigroup.com/en-GB/standards/bs-95009-procurement-in-the-public-sector/

evaluation, only as one input into the analysis; as such the position of each label can only be seen as an approximation of the average score given.

It is not surprising that proposals tended to be either seen as feasible *and* urgent or less feasible *and* less urgent as urgency and feasibility are not fully separable. It is also not the case that those proposals seen as less urgent are necessarily less important, so this exercise did not provide a tool to eliminate proposals entirely. However, the importance of sequencing the proposals and identifying priorities which could be quickly applied, versus more complex ideas that might take longer was valuable.

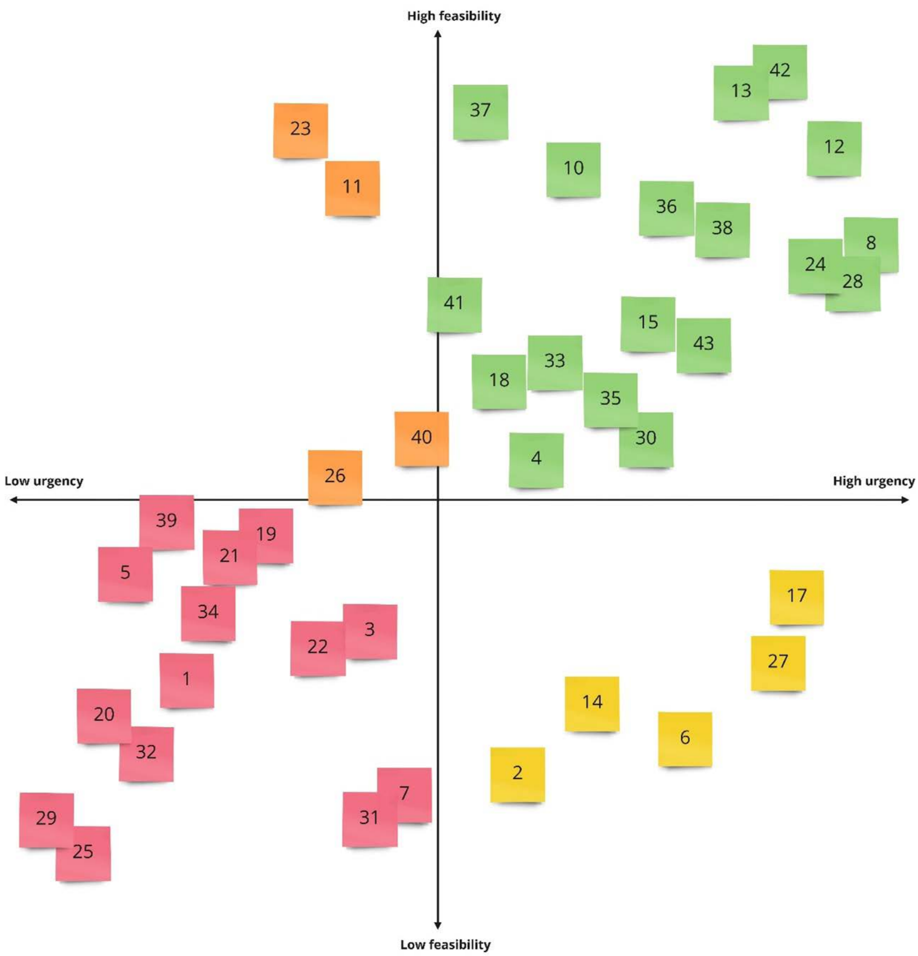

Figure 2. Purpose Labs participants' feedback on the feasibility and urgency of the proposals (numbered as in the list in Section 1 of this article). The horizontal position of the label approximately illustrates the average urgency score given by participants from low to high, left to right. The vertical position of the label approximately illustrates the average feasibility score given by participants from low to high, bottom to top.

Conclusion

The Future of the Corporation programme produced 17 academic papers involving more than 40 researchers, it engaged over 200 experts in 29 deliberative, evidence-generating roundtables and 100 stakeholders in the eight Purpose Labs described by this article. The thousands who have attended events, asked questions and voted with their feet have helped create the momentum needed for this programme to progress, while a small group of leaders have contributed extensive insight and knowledge throughout to guide the programme to its conclusions. It has been a deliberative, inclusive and stakeholder-driven exercise and this article describes the labs in detail in order to provide those interested in the programme the means of understanding some of the processes used and inputs considered.

The findings of the Purpose Labs described in this paper fed into the development of the proposals that made up the final report of the programme, *Policy & Practice for Purposeful Business*. The importance of acting on these proposals becomes clear with each passing year and as the recent COP26 talks have demonstrated, there is a growing need for clear thinking, based on evidence from a range of academic disciplines and practitioners, that reshapes our institutions to meet the needs and challenges of the 21st century.

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To cite the article: Bailey, J., Barratt, L., Morgan Jones, M. & Richards, H. (2022), 'Findings of the Future of the Corporation "Purpose Labs"', *Journal of the British Academy*, 10(s5): 17–41.
https://doi.org/10.5871/jba/010s5.017

Journal of the British Academy (ISSN 2052–7217) is published by
The British Academy, 10–11 Carlton House Terrace, London, SW1Y 5AH
www.thebritishacademy.ac.uk

Journal of the British Academy, **10(s5)**, 43–86
https://doi.org/10.5871/jba/0010s5.043
Posted 26 August 2022

The Future of the Corporation: the avenues for legal change

Dalia Palombo

Abstract: This article aims at analysing what could be the legal avenues to frame the future of the corporation. It focuses on fulfilling the Purpose and Do No Harm Objectives. The Purpose Objective should re-connect directors, shareholders and stakeholders in order to ensure that businesses rediscover their original function to serve the needs of society. To meet this goal, the article proposes changes in the laws regulating corporate governance. The future company could adopt a pluralistic approach, considering stakeholders fundamental actors, along shareholders and the board, in its corporate governance. The Do No Harm Objective should ensure that businesses are accountable when they damage the stakeholders affected by their activities. In order to meet this goal, the article proposes the introduction of enforcement mechanisms that would allow stakeholders to effectively enforce their rights.

Keywords: Corporation, purpose, harm, director's duties, shareholders, stakeholders, enforcement, control, accountability.

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The problems and objectives

A multinational enterprise could be defined as: '[a] cluster of corporations of diverse nationality joined together by ties of common ownership and responsive to a common management strategy' (Vernon 1968: 114; Vagts 1970: 740; Bartlett *et al.* 2003: 65). The status of multinational enterprise, being at the same time one economic unit and a conglomerate of separate legal entities, creates a gap between each separate company and the corporate group. While the multinational enterprise is able to use the complex structure of its transnational business to its advantage, the stakeholders affected by its activities have limited opportunities to influence its conduct. This results in two problems that could be defined the accountability and control gap.

The accountability gap

From the legal perspective, the activities of multinational enterprises are highly deregulated. Multinationals lack legal personality at both the international and national level. Hard laws are able to regulate only the activities of the single entities that are part of a corporate group. Soft laws recognise the relevance of multinationals but have no prescriptive authority over companies. This creates an accountability gap that has been widely discussed among scholars, businesses as well as international institutions (Jägers 2002; 2011; De Schutter 2005; Enneking 2012).

The obligations of a company that is part of a multinational enterprise could be found in domestic laws, international laws, and soft laws. Domestic laws would usually include tort laws, administrative laws, and criminal laws, depending on the various national legal systems. Such rules would typically apply only to single companies that are part of a corporate group and are incorporated in one country (Muchlinski 2021). International laws are traditionally applicable only to States and not to private entities, including companies. However, given the increasing importance of non-state actors in the international arena, a number of scholars have argued that international law, and specifically human rights, could apply also to non-state actors, including corporations. International law has the advantage to be theoretically applicable transnationally. However, the application of international laws to non-state actors is still uncertain and highly debated (Thomas 2000; Knox 2008; Karavias 2013). Soft laws are designed to apply to multinational enterprises, but they are not binding and therefore they do not establish proper obligations, but only non-legal responsibilities for companies (Deva 2003; Davarnejad 2011; Wettstein 2015).

All of the above laws can be typically enforced only at the national level. This is apparent given that there is no international court, arbitration tribunal, or any other treaty body that can enforce international law against companies. Therefore, even those who argue for human rights to apply to companies, would need domestic causes of actions to enforce them. There are, however, two main limitations to the implementation of domestic laws to multinational enterprises. First, domestic laws are designed to apply domestically and, therefore, their extraterritorial application is complicated and uncertain (Wouters & Ryngaert 2008; De Schutter 2010; Bright 2013; Aristova 2016). Second, multinational enterprises include several companies in various relationships with each other. They could be in a relationship of subsidiaries and parent companies or part of supply chains. In both cases, each company is a legal entity separated from the others and no company would be responsible for the actions of other corporations belonging to the same corporate group. This substantially reduces the chances to hold them accountable as each entity may have a different level of involvement and responsibility in the violation of the law (Blumberg 1985; Hansmann & Kraakman 1991; Leebron 1991; Skinner 2015).

The control gap

There is a second problem related to the globalisation and size of enterprises. There is an increasing gap between directors, shareholders, and stakeholders. Business and legal academics have widely analysed the separation between ownership and control of the company. In essence, shareholders are increasingly investing in widely held companies of which they own a very small fraction. They are often not involved in the management of the company, which is instead handled by professionals. This separation generates what has been defined as the first agency problem because the principals and owners of the company (the shareholders) are not capable to properly control the work of the agents (the directors) (Davies & Gower 2008: 365–648; Kershaw 2012: 171–88).

Scholars also defined a second agency problem facing a shareholder, who is de facto able to control the company, and minority shareholders, who do not have the relevant information to manage the company. The controlling shareholder has enough power to remove the board and instruct it to act in its interest, which may not necessarily align with the interests of minority shareholders. For example, a controlling shareholder may be interested in the long-term profitability of the enterprise and willing to incur losses in the short term, while minority shareholders are typically interested in the short-term profit and avoiding losses. The directors, in this case, are the arbiters of the second agency problem as they decide how to strike the right balance between the divergent interests of various shareholders. Nevertheless, their position may also be conflicted if the shareholder is de facto controlling the board (Davies & Gower 2008: 649-708).

There is another, less studied, third agency problem: the gap between businesses and society. Understanding this problem depends on the theory of the corporation that one marries. According to the concession, fiction or real entity enterprise theory, society encourages entrepreneurs to start a business because enterprises are likely to provide the best available goods and services in a competitive market. In this sense, businesses are agents of society (Bowen 1953; Phillips 1994; Kraakman *et al.* 2009: 35–63; Lan & Heracleous 2010). Nevertheless, there are alternative approaches to the origins of corporations. For instance, according to the aggregate theory, corporations are nexuses of contracts. The main question is who the parties to these contracts are. If the parties are only the shareholders, corporations cannot be considered agents of society because companies exist regardless of society (Carroll 2009; Chaffee 2017; Schmiel 2019). Instead, if the contractual parties are shareholders and stakeholders, such as consumers or employees, then the third agency problem could still be defined as the problem of control that stakeholders (as principal) should exercise over corporations (as agents) (Schwartz 1993: 411–13; Phillips 1994; Ponoroff 1994: 465–74; Kraakman *et al.* 2009: 29–47, 110–119). The example below could better illustrate the third agency problem also with respect to the impact that globalisation has on businesses.

Consider a small village where there is a state monopoly on shoes. The state has no incentive to make particularly cheap, good, stylish or comfortable shoes because nobody would be able to buy better shoes than the one it provides. Instead, if the village is a competitive market, where ten different shoe shop corporations are competing with each other, each of them will strive to offer the best shoes at the lowest possible price. Consumers and employees would be better off because each industry would aim at providing the best shoes and, in order to do so, would have to employ villagers. However, if one of these businesses would unreasonably pollute the environment or pay its employees extremely low wages, villagers who are at the same time people living around the shoe industry, working for such factory, consumers and shareholders of such company, would likely react to the pollution or low pay because it would affect them directly. The village would exercise a certain level of control over the activities conducted by the ten shoe shop corporations working there.

However, the situation drastically changes if the shoe shop is a multinational enterprise marketing its goods in one part of the planet (assume Europe), producing in a second one (assume Asia), being widely held by shareholders from all over the world. The management of the group would be inevitably detached from the problems that stakeholders face in various countries where the group operates. Most shareholders would not exercise control over the directors and would focus on the short-term value of their shares; most directors would concentrate on the expected returns that the company would generate; most consumers would be interested in the price and quality of their shoes, rather than in the conditions in which they were made; and most workers and third parties affected by the production would be at the periphery of the group and unable to exercise any control on it.

Essentially, while business has gone global there is not yet a global society able to exercise effective control over transnational enterprises. One could argue that with globalisation and technological advances, a global society is emerging. NGOs, consumers protection organisations, human rights, and environmental advocacy are increasingly exercising the type of control that is necessary to ensure that multinational enterprises respond to the needs of people (Koh 1996; 2006). However, given the current backlash against cosmopolitanism, this aspiration seems, at least for the moment, not yet sufficiently developed to exercise effective control over multinationals. The discrepancy between the freedom multinational enterprises enjoy and the lack of control that society can exercise over them establishes a gap that is increasingly perceived as unacceptable by society and unsustainable to the environment (Deva 2003; Wettstein 2015).

The Future of the Corporation programme

There are two main problems related to multinational enterprises: an accountability gap and a control gap. It is difficult for society to both hold multinational enterprises accountable for their actions, and exercise control over their activities so that they benefit people.

Against this background, the Future of the Corporation programme aims at understanding how businesses should be structured in the future to meet the needs of an increasingly global society. A fundamental part of such restructuring would be a change in the law that should address the problems identified above. Any proposed change in the law should aim at fulfilling the following two objectives:

1) the Purpose Objective – enterprises should aim at producing profitable solutions to the problems of people or planet;
2) the Do No Harm Objective – enterprises should not profit from producing problems for people or planet.

The Purpose Objective should re-connect directors, shareholders and stakeholders in order to ensure that businesses rediscover their original function to serve the needs of society. The Do No Harm Objective should ensure that businesses are accountable when they damage the stakeholders affected by their activities.

This article aims at analysing what could be the avenues for legal change that would help meet these two objectives. Legal changes alone will not achieve the Purpose and Do No Harm Objectives, as a much broader cultural change is necessary in order to configure the corporations of the future. Nevertheless, law has the fundamental function to demark acceptable and non-acceptable behaviour in society (Hart 2012; Dworkin 1967). Therefore, legal changes would be a fundamental tool to help achieving the Purpose and Do No Harm Objectives. The focus of this article is on possible legislative changes of UK law, although other jurisdictions are also taken into account.

Principle 1

Corporate law should place purpose at the heart of the corporation and require directors to state their purposes and demonstrate commitment to them

Principle 1 suggests placing purpose at the heart of UK company law, with a particular focus on changing the text of Section 172. This section of the article analyses first what these changes could be, and second if the proposed changes would be sufficient to develop a multi-stakeholder corporate governance model that would appropriately connect shareholders, directors and stakeholders.

Changes to Section 172

The following section compares the current version of Section 172 with a possible new draft that has been taken into account by the Future of the Corporation programme.

Current Section 172

> (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.

(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.

Obligations

Sec 172 is regarded as part of the duty of loyalty in the UK (Davies and Gower 2008: 506–525). There are two obligations of directors enshrined in current Sec 172: 1) the obligation *to 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 2) the obligation to *have regard (amongst other matters) to (a)-(f).* Obligation 1) requires directors to act in the interest of shareholders. Obligation 2) requires directors to conduct appropriate due diligence in considering the interests of stakeholders while pursuing the benefit of shareholders. For example, if a director finds that the interest of shareholders is contrary to the one of stakeholders, s/he must act in the interest of the shareholders. Instead, if the interest of shareholders could be aligned with the one of stakeholders, then the director should find a synthesis between these various interests.

Standards

The current standard adopted by Sec 172 is a mix of objective and subjective. First, as it pertains to obligation 1), the liability of a director should be tested on the basis of whether there was any rational reason to make a certain decision (subjective standard). Second, as it pertains to obligation 2), the liability of a director should be tested against how the average reasonable director would have had regard to the interests of stakeholders (objective standard) (Kershaw 2012: 334–86).

A subjective standard is, generally speaking, regarded as lower than an objective standard. If one applies a subjective standard, it is enough for directors to find one rational reason to justify their actions as aimed at promoting the success of the company for the interest of shareholders.[1] Instead, if one applies an objective standard, it is not sufficient for a director to find one rational reason that would justify his/her

[1] This concept would be referred to as the business judgment rule in the US. See *Regentcrest plc v Cohen* [2001] BCLC 2 80.

choice. The decision must be compatible with the one that an average director would have made.

At first look, therefore, the standard against which directors are assessed is lower as it pertains to the obligations towards shareholders and higher as it pertains to the obligations towards stakeholders. However, this is only an illusion. In fact, while the directors have a duty to act for the shareholders' benefit (obligation 1), they only have a duty to have regard to stakeholders' interests (obligation 2). Therefore, the fact that the standard applicable to such an obligation is objective, is of little value because in any case all an average reasonable director needs to do is to take into consideration the costs an activity would have on the stakeholders.

Corporate groups

Sec 172 is not prescribing the duty of directors in respect of companies that are part of a corporate group. Such a duty is still defined by the common law. A director must act in good faith in the best interest of the company. However, given that the company is part of a corporate group, the interest of the group is fundamental to the company's benefit.

The standard is objective: a director must act in accordance with how the average reasonable director would have acted in the best interest of the company within the corporate group. Note that an average reasonable director would typically take into high consideration the interest of the group in determining the best interest of the company.

Therefore, there is a formal discrepancy between the subjective standard applicable to directors managing a company (Sec 172) and the objective standard applicable to directors of a company which is part of a corporate group. Nevertheless, the discrepancy between subjective and objective standards does not result in a substantial difference in the treatment of directors because an average director of a company that is part of a corporate group would de facto take the interest of the group into account. Although the standard is objective, it is not more demanding than the subjective standard of Sec 172 (Davies & Gower 2008: 515–16; Kershaw 2012: 348–51).[2]

Draft new Section 172

> A director of a company must act in the way that he considers, in good faith, would be most likely to promote the ~~success~~ purposes of the company. ~~for the benefit of its~~

[2] Charterbridge Corporation Ltd v Lloyds Bank Ltd [1969] 2 All ER 1185.

~~members as a whole~~. In defining its purposes, a company must have fair regard (amongst other matters) to

(a) the benefit of its members as a whole;
(b) the likely consequences of any decision in the long term,
(c) the interests of the company's employees,
(d) the need to foster the company's business relationships with suppliers, customers and others,
(e) the impact of the company's operations on the community and the environment,
(f) the desirability of the company maintaining a reputation for high standards of business conduct, and
(g) the need to act fairly as between members of the company.

The purposes of the company must represent a variety of interests.
If a company is part of a corporate group, the above obligations apply also in respect of the corporate group.

Obligations

The draft of the new Sec 172 introduces purposes as the company's driver. It establishes two separate obligations:

1) The director's obligation to promote the purposes (instead of the success) of the company;
2) The company's obligation to define purposes having regard to the factors mentioned in (a) to (g).

Obligation 1) would detach the director's duty from the interest of the shareholders reproducing a logic similar to the one of the laws of other jurisdictions.[3]

Obligation 2) would require the company to define purposes taking into account a variety of interests. Therefore, the meaning of the word 'regard' would be substantially different from current Sec 172, where directors just have to exercise due diligence. This would be an innovative step, if compared to other jurisdictions which allow, but do not require, directors to act in the interest of stakeholders.[4]

A critical question would be what the duty of directors is in respect of obligation 2). Would directors have a duty to define purposes or would this duty be left to the shareholders? The language of the draft leaves this question open in order to provide different solutions to various companies. While public companies may prefer to have

[3] See infra New York Business Corporation Law Sec 717 or 2005 Connecticut Code Sec 33–756.
[4] ibid.

the directors defining the company's purposes, in private companies, shareholders may be those defining purposes. Each company could determine this aspect in its articles of association.

A possible critique of this approach could be that shareholders would be able to define the purposes of the company in narrow terms focusing on their self-interest. The alternative could be then to specify in the law that it is for directors to define purposes. This would set up the definition of purposes as part of directors' duties and take the power to define purposes away from the shareholders. While this would limit the opportunities for shareholders to define the purposes of the company in their interests, it would also reduce the flexibility that companies may want in terms of delimitating and defining the respective roles of shareholders and directors.

A 2018 reform of the UK Corporate Governance Code adopts a similar approach empowering directors to define purposes. The Corporate Governance Code is a comply or explain set of principles. It applies only to companies with a Premium Listing of equity shares. This means that non-premium listed corporations can disregard it without explanation, and premium listed companies may avoid compliance with the Code if they provide for a reason.[5]

Scholars have questioned the effectiveness of such a reform given the current language of Sec 172 of the Companies Act. In fact, current Sec 172 (1) establishes shareholders primacy, while Sec 172 (2) states that a different company purpose could be set. The preferred view is that directors could define the purposes of the company only within shareholders primacy, and therefore only if shareholders would allow them to do so. Accordingly, Sec 172 (2) restates the common law position that shareholders could agree to establish a different corporate purpose (Kershaw & Schuster 2021: 488–90).

This concern would, however, be resolved by the revised text of Sec 172 which would erase shareholders primacy. Therefore, if such a reform would be adopted, unless otherwise decided and motivated, directors of premium listed companies should define the purposes of the company having fair regard to various interests and promote them. If instead the company would provide for an explanation to diverge from the Corporate Governance Code, shareholders could define purposes, but it would still be for directors to promote them.

A related issue is what could be the procedures for a company to define their purposes. This should be left for each company to decide and not legally imposed. However, a possibility could be to suggest in the Corporate Governance Code that directors establish a committee in charge of meeting with the various stakeholders

[5] *UK Coporate Governance Code*, 2018, Principle 1.

that are or could potentially be affected by the activities of a company, as well as with the shareholders, in order to strike a fair balance between various interests.

Corporate groups

The new draft of Sec 172 should also clarify the directors' duties in respect of companies that are part of a corporate group. The aim of this provision should be to avoid that each company that is part of a corporate group defines its own purposes in narrow terms while disregarding the purposes of the whole group. In this instance, directors could be held to account only against the purposes of a specific company without bearing any responsibility for the overall activities of the group. This would reproduce the accountability gap of multinational enterprises. Therefore, it would be commendable to ensure that each company belonging to a corporate group, would have to:

1) define the purposes of the company;
2) define the purposes of the corporate group;
3) ensure that such purposes are consistent with each other; and
4) require the directors to promote both purposes.

Standards

Another fundamental question would be whether the standard applicable to the directors' obligations would be objective or subjective.

As it pertains to obligation 1), the standard would be subjective by analogy to what UK law has already established concerning current Sec 172 duty to promote the success of the company.

As it pertains to obligation 2), unless specified in the new draft of Sec 172, it would be more difficult to assess what kind of standard UK courts would apply. As explained above, an objective standard is currently applicable to the obligation of directors to have regard to the interests of stakeholders. Therefore, one could think that the same standard would apply also to obligation 2) in the new draft of Sec 172. However, the new obligation would be substantially different from the duty of current Sec 172. While the current duty refers to a mere due diligence obligation, the new duty would be an obligation requiring directors not only to take into account other interests, but to define and promote the purposes of the company in the interests of a variety of actors. Therefore, UK courts may no longer apply an objective standard to such a new obligation to define purposes and may opt to apply a subjective standard.

In this analysis of various standards applicable to directors, there is an additional element to take into account. As explained above, the standard currently applicable to directors of companies that are part of a corporate group is objective as defined by the common law.

Against this background, the new Sec 172 should aim at levelling such discrepancies that would require directors to have potentially two different liabilities when promoting the purposes of the company and the group, as well as two different liabilities when defining and promoting the purposes of the company.

Critiques

There are three main critiques that one could raise as it pertains to the proposed changes of Sec 172. First, that the proposed changes go too far in terms of erasing shareholders primacy. Second, conversely, that such changes would not be enough to overcome shareholders primacy. Third, that overcoming shareholders primacy would not ensure that businesses rediscover their original function to produce profitable solutions to the problems of people or planet.

Too much

A possible criticism of the proposed changes in Sec 172, could be that they go too far in erasing shareholders primacy. In fact, there are a number of proposals for modifying Sec 172 to encourage companies to adopt a socially responsible purpose. However, most proposals do not typically erase shareholders primacy but attempt to combine shareholders primacy with other interests. For example, the Better Business Act 2021[6] argues for a purpose approach similar to the one proposed in this article. However, it also adds a section that attempts to balance shareholders primacy with other interests, instead of erasing it.

> (2) The purpose of a company shall be to benefit its members as a whole, whilst operating in a manner that also —
>
> (a) benefits wider society and the environment in a manner commensurate with the size of the company and the nature of its operations; and
>
> (b) reduces harms the company creates or costs it imposes on wider society or the environment, with the goal of eliminating any such harm or costs.

[6] 'The Better Business Act' (*Better Business Act*) <https://betterbusinessact.org/> accessed 18 September 2021.

These proposals mirror the 2013 reform of Indian law, which passed from shareholder primacy to promoting the interests of shareholders alongside the ones of stakeholders. Sec 166(2) of the Indian 2013 Companies Act states:

> (*2*) A director of a company shall act in good faith in order to promote the objects of the company for the benefit of its members as a whole, and in the best interests of the company, its employees, the shareholders, the community and for the protection of environment.

Although this change had the commendable objective of encouraging companies to be more socially responsible, commentators criticised such an approach as vague. It is essentially unclear what directors have to do and if shareholders' benefit shall be considered more relevant than stakeholders' interests. The cost of retaining shareholders primacy but aligning it with other interests, is that directors will not know if shareholders may sue them for breach of duties when they fulfil the stakeholders' interests. Thus, if the reform of Sec 172 does not erase shareholders primary, a director would find him/herself in the following situation: to act for the benefits of shareholders would not result in substantial legal risks, but to act in the interests of stakeholders may expose him/her to lawsuits. This alone would create an incentive for directors to continue to act in the interest of shareholders (Afsharipour 2017).

Not enough

The proposed changes risk to create just a Sec 172 out of tune with the rest of UK company law, instead of shifting from shareholders primacy to a multi-stakeholders approach, aimed at incorporating a variety of interests in corporate governance. It is sufficient to compare UK company law with the jurisdictions of the United States, to understand that a complete change of paradigm would be required to overcome shareholders primacy. Table 1 compares the different balance of powers between shareholders and board in the UK and Delaware. This is not a comprehensive analysis of the two corporate laws, but it summarises the main differences of the two systems that make some scholars define the UK a shareholders primacy and Delaware a directors primacy jurisdiction (Kershaw 2012: 189–233).

Table 1. Comparison of balance of powers between shareholders and board in UK and Delaware.

United Kingdom	*Delaware*
Art 3 Model Articles: shareholders may delegate the power to the board	Sec 141 Delaware General Corporation Law: The power of the board of directors is undelegated and original
Sec 303-305 Companies Act: Right to Call a General Meeting 1) Minimum 5% of voting shares request directors to call a meeting 2) Directors are under a duty to call a meeting in 21 days 3) If the directors do not call the meeting the shareholders who requested the meeting can call it themselves 4) All reasonable expenses are on the company	No such right exists in Delaware
Sec 314 Companies Act: Right to Communicate 1) Minimum 5% of the total voting rights or at least 100 members with voting rights and shares for at least 100 GBP each 2) Statement should be no more than 1000 words	No such right exists in Delaware
Art 4 Model Articles: Instruction Rights shareholders can instruct directors by a special resolution (75%)	No such right exists in Delaware
Sec 21 Companies Act: Change Articles of Association by special resolution (75% of the votes)	Sec 242 Delaware General Corporation Law: Change of the Certificate of Incorporation 1) Board must propose the amendment 2) Shareholders vote by the majority of the issued shares
Removal of Directors All directors are appointed for 1 year. Sec 168 Companies Act: To remove a director it is necessary an ordinary resolution (50%+1 votes).	Sec 141 (k) Delaware General Corporation Law: Removal of Directors: 1) NON-CLASSIFIED BOARD (1 year appointment): To remove a director it is necessary the majority of the vote cast without cause. 2) CLASSIFIED BOARD (3 years appointment): To remove a director it is necessary the majority of the vote cast with cause.
Non-Frustration Rule (EU Takeover Directive Article 9 and UK City Code on Takeovers Articles 9, 21)	Take Over Defences are allowed within certain limits determined by the case law

As illustrated by this table, in the UK shareholders delegate the power to the board, have numerous rights to intervene in the activities of the board, can change the articles of association with the agreement of 75% of their body, while directors are appointed only for one year and can be removed without cause. Instead, in Delaware, the law empowers the board; shareholders have no rights to instruct the board; in order to change the certificate of incorporation the board must propose an amendment (de facto controlling any change); and most boards would be staggered, where directors are appointed for three years and removable only with cause. In addition, take-over defences are available in Delaware and not in the UK. Therefore, in order to remove shareholders primacy from UK company law a structural change of paradigm would be required.

Does this improve the social responsibility of businesses?

There is, however, a more significant concern in respect of the debate on shareholders primacy: the divergent approaches adopted by the UK and the US do not seem to result in practical differences in terms of the social responsibility of companies. This could be better exposed by the comparison between NY and UK law.

> New York Business Corporation Law Article 7, Sec 717:
>
> (a) A director shall perform his duties as a director, including his duties as a member of any committee of the board upon which he may serve, in good faith and with that degree of care which an ordinarily prudent person in a like position would use under similar circumstances. (…)
> (b) In taking action, including, without limitation, action which may involve or relate to a change or potential change in the control of the corporation, a director shall be entitled to consider, without limitation,
>
> (1) both the long-term and the short-term interests of the corporation and its shareholders and
> (2) the effects that the corporation's actions may have in the short-term or in the long-term upon any of the following:
>
> (i) the prospects for potential growth, development, productivity and profitability of the corporation;
> (ii) the corporation's current employees;
> (iii) the corporation's retired employees and other beneficiaries receiving or entitled to receive retirement, welfare or similar benefits from or pursuant to any plan sponsored, or agreement entered into, by the corporation;
> (iv) the corporation's customers and creditors; and
> (v) the ability of the corporation to provide, as a going concern, goods, services, employment opportunities and employment benefits and otherwise to contribute to the communities in which it does business.

> Nothing in this paragraph shall create any duties owed by any director to any person or entity to consider or afford any particular weight to any of the foregoing or abrogate any duty of the directors, either statutory or recognised by common law or court decisions.

It is apparent from the comparison between Sec 717 of the NY Business Corporation Law and Sec 172 of the UK Companies Act, that NY law allows directors to act in the interest of any stakeholders, while UK law requires the board to act in the shareholders' interest. However, there are several practical factors that level the divergent approaches that UK and NY law took.

First, in widely held companies, shareholders are often rationally apathetic. Therefore, although they can theoretically exercise several rights in the UK, in practice they do not. This makes the functioning of UK and NY corporations not that far apart from each other. Furthermore, in both jurisdictions, directors tend to act in their self-interest (instead of in the one of other stakeholders) in cases of rational apathy. Therefore, switching from a shareholders to a directors primacy jurisdiction may simply intensify the first agency problem, without being of particular help to stakeholders (Friedman 1973; Kershaw 2012: 171–88).

Second, directors owe the duties of care and loyalty to the company. However, in both the UK and NY, the only persons that are entitled to sue directors are shareholders. The ability of shareholders to sue directors is a reason for the board to act primarily in the interest of shareholders in both jurisdictions.[7]

Third, the only persons who can elect and remove directors are in both jurisdictions the shareholders. This is a sufficient incentive for directors to act primarily in the interest of shareholders.[8]

Fourth, often a part of the directors' compensation is constituted by options to buy shares in the company which they manage. For example, more than 60% of the compensation of the CEOs of S&P 500 companies consists of equity-based compensation (Larcker and Tayan, 2019). As a result, directors will have interests that are mostly aligned with those of the shareholders.

Therefore, both in NY and in the UK, boards act primarily in the interest of the shareholders or in their self-interest, often ignoring the interests of third parties because neither NY nor UK laws create appropriate incentives for the directors to care about the interests of stakeholders. Scholars identified these as the primary reasons for corporate laws to fail society's interests: no matter whether the corporate legal system could be classified as shareholders or directors primacy, the directors will pursue the interests of shareholders, because they have no incentives to do otherwise.

[7] Compare Companies Act Sec 260–269 and NY Business Corporation Law Sec 626.
[8] Compare Companies Act Sec 157–169 and NY Business Corporation Law Sec 703–706.

Shareholders primacy is so embedded in corporate culture that most directors believe that maximising shareholders value is the sole purpose of the company (Sjåfjell, 2020).

However, there is a critical difference between the UK and NY approaches as it pertains to those directors that want to act in a socially responsible way. In NY, a director who wants to act in the stakeholders' interest, even if this could result in negative externalities for the shareholders, is able to do it. His/Her duty is to the company and if s/he believes that pursuing the stakeholders' interest is also in the interest of the company, s/he can pursue such an interest. Instead, in the UK, directors (unless otherwise decided in the articles of association by the shareholders, Sec 172. 2) have to promote the success of the company for the benefit of the shareholders. This means that if a director believes that the interests of the company are aligned with those of stakeholders, but not with the benefits of shareholders, s/he cannot act in the interest of the former and to the detriment of the latter. Acting to the detriment of shareholders would be a breach of the duty to loyalty as enshrined in Sec 172. A director would, therefore, not act in the stakeholders' interest, unless such an interest would also benefit the shareholders.

Principle 2

Regulation should expect particularly high duties of engagement, loyalty and care on the part of directors of companies to public interests where they perform important public functions

Principle 2 would ensure that licensed companies, which are deemed to perform a public function, would define their purposes according to their public role. This could be achieved by adding a paragraph in Sec 172.

> Draft new Sec 172 (2)
> In defining its purposes, a licensed company must reflect its public role.

For example, a bank will have to define its social purposes within its overall licence to hold the customers' money. Therefore, the bank would have to define its purposes:

1) within its function to hold people's money, and therefore, for example, it should limit its investment in high risk carrying activities that would result in a substantial loss of the public money;
2) taking into account, like all other companies, the factors included in Sec 172 (1) (a)-(g) – for example, by considering whether to invest in the renewable energy sector rather than in coal.

A question arises as to whether the new Sec 172 (2) would truly add anything to businesses that are already highly regulated. For example, the investment policies of banks are already regulated without the need to include such policies into corporate purposes.[9] However, there would be at least an advantage to include such considerations into the corporate purposes. The requirements linked to the company's public function would become part of the directors' duties, instead of a regulation applicable to the company. This means that directors could be personally liable if they do not promote the purposes of the company.

In this sense, directors would have duties similar to those prescribed by public benefit corporations in some US states. A public benefit corporation is incorporated by the shareholders with the purpose to produce a public benefit. The incorporation of such a company is a choice that shareholders may make which is unrelated to the license the company may own. Nevertheless, once a public benefit corporation is incorporated, its directors would have a duty to balance the public benefit defined in the certificate of incorporation with all other interests at stake. For example, Delaware General Corporation Law defines the directors' duties as follows:

> **§ 362 Public benefit corporation** defined; contents of certificate of incorporation.
> A "public benefit corporation" is a for-profit corporation organized under and subject to the requirements of this chapter that is intended to produce a public benefit or public benefits and to operate in a responsible and sustainable manner. To that end, a public benefit corporation shall be managed in a manner that balances the stockholders' pecuniary interests, the best interests of those materially affected by the corporation's conduct, and the public benefit or public benefits identified in its certificate of incorporation.

The proposed amendment of Sec 172 (2) of the Companies Act in the UK would establish a similar duty for directors to balance the public function of the company with the other interests at stake. However, unlike in Delaware, in the UK such a public function would not be defined by the certificate of incorporation, but by the license the company owns.

It is still doubtful whether this approach would add much to the already regulated sector of licenses because directors already have a duty to follow such regulations as part of their duty of care (Sec 174).[10] Nevertheless, in the context of the legislative

[9] See e.g. Financial Services and Markets Act 2000, Capital Requirements Directive (2013/36/EU), Capital Requirements Regulation (575/2013).

[10] Sec 174 '(1)A director of a company must exercise reasonable care, skill and diligence. (2)This means the care, skill and diligence that would be exercised by a reasonably diligent person with—(a)the general knowledge, skill and experience that may reasonably be expected of a person carrying out the functions carried out by the director in relation to the company, and (b)the general knowledge, skill and experience that the director has.'

amendments proposed to Sec 172 (1), Sec 172 (2) would require that the corporate purposes of licensed companies would be centered around the company's license. This approach would certainly ensure consistency between the corporate laws and regulations applicable to companies and the board.

Enforcement mechanisms: Do No Harm

The new version of Sec 172 would certainly be of help in terms of switching the focus of UK company law from shareholders primacy to a pluralistic approach. It would also go a step further than Sec 717 of NY Law as it would not only allow, but also demand, directors to promote a variety of interests which do not include only those of shareholders. Nevertheless, the proposed changes would not be sufficient to overcome shareholders primacy because, as explained above, the whole structure of UK company law is constructed around shareholders. Furthermore, even if one could potentially achieve a change of paradigm, this would certainly allow the board to make decisions in the interest of stakeholders (pursuing potentially the Purpose Objective), but would not prescribe any obligation towards stakeholders, let alone sanction companies that profit from producing problems for people and planet (not pursuing the Do No Harm Objective). In this respect, scholars identified the lack of enforcement and sanctioning mechanisms enabling stakeholders to hold the board to account as one of the main barriers that prevent companies from working for the benefits of society, even in directors primacy jurisdictions (Friedman 1973; Afsharipour 2017; Sjåfjell 2020; Ruggie *et al*. 2021). Thus, in order to meet, at the same time, the Purpose and Do No Harm Objectives, it is necessary to take into account further changes that could be combined with new Sec 172.

The following propositions are by no way comprehensive. A legislator could take into consideration a number of other avenues to ensure the Do No Harm Objective. However, these are a few possibilities that the Future of the Corporation Programme has taken into account in order to achieve the Do No Harm Objective.

Control approach: internalising stakeholders interests

A possible avenue to enforce the proposed new draft of Sec 172 in the interest of all stakeholders, could be to internalise their concerns in the corporate governance of the company. If stakeholders become, alongside directors and shareholders, part of the company, then directors will have to take their interests into account in their decision-making process.

There could be numerous avenues to achieve such a result because stakeholders are currently not controlling any aspect of the company's life. The control of corporations is divided between the shareholders and the board. These two groups are traditionally perceived as the two components of a company. They shall, on the one hand, cooperate to achieve the success of the company, but are, on the other hand, in a potential conflict of interest (first agency problem). A much wider range of stakeholders that are also contributing to the existence and functioning of the company are kept at its margins and exercise no control over it (Veldman & Willmott, 2016). Against this background, any change in the law that would allow some form of control of the stakeholders over the board, would represent a step forward.

Three mechanisms that could have a relevant impact in terms of stakeholders' control are: the possibility for stakeholders to file lawsuits against directors on behalf of the company (derivative actions), or on their own behalf (oppression remedy), and the appointment of some members of the board by stakeholders (co-determination).

Derivative actions

Managing a company includes deciding when and under which circumstances such a company may file a lawsuit against third parties. Directors, therefore, typically make such an assessment and are able to file suits on behalf of the company. However, a problem arises as to how a company may sue the directors for breach of their duties. In fact, directors owe their duties of loyalty and care to the company. If they breach such duties, they would first of all damage the company and only indirectly damage the shareholders. In this scenario, when a company may need to sue the board, it is apparent that the directors will not sue themselves. It may be possible that some directors may sue others, but this is an unlikely scenario because they would have to sue their colleagues for breach of duties. For this reason, despite filing a lawsuit on behalf of the company is a business decision, UK law exceptionally allows any shareholder to sue the directors on behalf of the company for breach of duties. It is evident, however, that by empowering any shareholder with a right to bring derivative suits, nuisance lawsuits could occur. To minimise the likelihood of abuse, UK law establishes a judicial check on any lawsuit a shareholder may want to file on behalf of the company. This mechanism is regulated by the Companies Act in detail and aims at balancing, on the one hand, the control that shareholders should exercise over the directors and, on the other, the inexperience or bad faith that such shareholders may have. There are still some concerns that one could have on the ability of the judicial branch to make a business decision, such as whether or not a company should file a lawsuit against its own directors, but at large this is believed to be a reasonable compromise to allow companies to file suits against directors (Reisberg 2005: 606–28; Davies & Gower 2008: 605–27; Kershaw 2012: 606–28).

Against this background, one of the problems that could make inefficient any change of Sec 172, is the lack of accountability mechanisms. Even assuming Sec 172 would require directors to act in the interest of society, why would they comply with such a law if no stakeholder could ever hold them to account? Shareholders may sue directors who run a company against their interests. However, shareholders would have little incentive to sue a director for not taking into account the interests of employees, the environment or the community living nearby an industry the company owns. To the contrary, often the interests of such stakeholders would be opposed to the one of shareholders (Keay 2016; Veldman & Willmott 2016). In widely held companies shareholders, who are increasingly detached from the management of the company and rationally apathetic, have little incentive to sue directors even when this could be in their self-interest, let alone suing directors to fulfil the interests of third parties. As a result, any change of Sec 172 could end up being ineffective in terms of achieving the Do No Harm Objective, because de facto the directors would have no incentive to take into account any interest other than their own and the one of the shareholders.

Therefore, a possible avenue for ensuring the enforcement of the new draft of Sec 172, would be to allow stakeholders to file derivative lawsuits on behalf of the company. Stakeholders could, like shareholders, sue directors who do not fulfil the purposes of the company or who define the purposes of the company without taking into account the interests (a)-(g) (which would be considered as a breach of their duty of loyalty); or for breach of their duty of care. In fact, according to Sec 174, 'a director must exercise reasonable care, skill and diligence' in any of its decision-making processes. This would include also those decisions that a director would make to promote the company's purposes.

Stakeholders as shareholders

Theoretically, any stakeholder could become a shareholder in a widely held company and sue a director for breach of duties. Therefore, provided that Sec 172 would change, including the Purpose Objective, stakeholders could simply be encouraged to pursue such a creative litigation strategy.

This is not simply a theoretical example. In a Polish case *ClientEarth v Enea*, ClientEarth, an NGO, bought some shares in the company Enea to challenge the construction of a coal power station as it would cause environmental risks with financial repercussions on the company and the shareholders. The NGO won the case in its capacity of shareholder.[11]

[11] *Client Earth v Enea* [2019] Regional Court in Poznań.

Although this route is possible, it would be commendable to establish a specific mechanism for stakeholders to file suits on behalf of the company to avoid some undesired outcomes. As explained above, in the UK it is for the judicial branch to assess whether a derivative lawsuit filed by shareholders is worth pursuing. If stakeholders would instrumentally buy shares in a company to file a derivative lawsuit, judges could accommodate such strategic litigation or close the door to it.

The Canadian example

Canada and Singapore allow derivative actions from any person who is identified as ‘proper’ at the court’s discretion. Potentially, any stakeholders can sue the directors for breach of duties (Calkoen 2019; Koh 2001; Ben-Ishai 2007). Some academics praised this approach as a possible avenue to ameliorate the mechanism of derivative actions in the UK. In fact, although shareholders can file derivative actions on behalf of the company, they rarely exercise such a right. This is due to a number of reasons, including the cost of litigation, rational apathy, and the fact that shareholders have alternative means to exercise control over the board or can simply exit the company by selling their shares in the market. Therefore, it is believed that allowing any person to sue the directors could reduce the agency problem and ensure that the board would act in the company’s interest, instead of in its own (Friedman 1973; Keay 2016).

Canada is often defined as the pioneer jurisdiction in terms of establishing a stakeholders-friendly corporate governance regime (Vasudev 2015). Importantly, the Canada Business Corporation Act allows any ‘proper person’ to file a complaint on behalf not only of the company but of any of its subsidiaries, enabling a potential influence of stakeholders also on corporate groups. However, in Canada, the judicial approach has been to carefully assess whether to permit stakeholders to file a lawsuit on behalf of the company: courts limited the number of persons who could be identified as ‘proper’ to file a complaint and focused on the business judgment rule (Ben-Ishai 2007). As a result, stakeholders filed a limited number of derivative actions in Canada. Some scholars have criticised such an approach, arguing that it is insufficient to ensure that stakeholders could exercise control over the board (Ben-Ishai 2006; Sarra 2006; Vasudev 2015). Against this background, an important issue to consider in establishing derivative actions for stakeholders in the UK would be whether the law should define a list of stakeholders that are entitled to file a lawsuit, instead of leaving such a definition for courts to decide on a case by case basis. Stakeholders include a wide variety of actors, from creditors, previous shareholders, previous directors to NGOs and employees. It would be, therefore, commendable to take these different roles into account and structure stakeholders’ derivative lawsuits accordingly.

It should be noticed in this regard, that in Canada derivative lawsuits filed by stakeholders are not connected with a duty of directors to promote the company's purposes, but instead with more general duties of loyalty to act in the corporation's best interest and of care.[12] However, if the UK were to adopt the new draft of Sec 172, and the duty imposed on directors would be to promote the purposes of the company and to define such purposes in the interests of various groups, this proposed legislation would be a step forward, if compared to Canadian law, in terms of ensuring that stakeholders would have an impact on the company's conduct.

Furthermore, Canada adopts an approach, similar to the one of US jurisdictions such as NY and Delaware, in contrast with the shareholder primacy approach currently enshrined by UK legislation (Ben-Ishai 2006; Vasudev 2015). This approach limits the possibility for shareholders to sue directors in order to allow the board to exercise more flexibility in the management of the company. Therefore, generally speaking, UK law establishes a higher standard of review of the directors' actions if compared with jurisdictions such as the US or Canada. This is because, being a shareholder primacy jurisdiction, the UK aims at reducing the first agency problem and at establishing more effective enforceability mechanisms available to shareholders. If such a standard would also apply to cases filed by stakeholders, the control exercise on directors would be more stringent than the one currently provided by Canadian law. This is especially true if the applicable standard would be objective instead of the subjective standard often adopted in Canada (business judgment rule). As explained above, in the UK both objective and subjective standards are currently applicable to directors depending on the duty that they are accused to breach.[13] Therefore, the introduction of derivative lawsuits for stakeholders would arguably be more effective in the UK than in Canada.

Sec 263

It would be fundamental to take into account Sec 263 of the Companies Act which regulates how judges should assess whether to grant shareholders permission to file a derivative lawsuit on behalf of the company.

> 263 Whether permission to be given
>
> (1) The following provisions have effect where a member of a company applies for permission (in Northern Ireland, leave) under section 261 or 262.
> (2) Permission (or leave) must be refused if the court is satisfied —

[12] Sec 122(1) Canada Business Corporations Act.
[13] In the UK the standards applicable to the duty of care (Sec 174) are typically higher than the one analyzed above as it pertains to the duty of loyalty (Sec 172).

(a) that a person acting in accordance with section 172 (duty to promote the success of the company) would not seek to continue the claim, or
(b) where the cause of action arises from an act or omission that is yet to occur, that the act or omission has been authorised by the company, or
(c) where the cause of action arises from an act or omission that has already occurred, that the act or omission —

(i) was authorised by the company before it occurred, or
(ii) has been ratified by the company since it occurred.

(3) In considering whether to give permission (or leave) the court must take into account, in particular —

(a) whether the member is acting in good faith in seeking to continue the claim;
(b) the importance that a person acting in accordance with section 172 (duty to promote the success of the company) would attach to continuing it;
(c) where the cause of action results from an act or omission that is yet to occur, whether the act or omission could be, and in the circumstances would be likely to be —

(i) authorised by the company before it occurs, or
(ii) ratified by the company after it occurs;

(d) where the cause of action arises from an act or omission that has already occurred, whether the act or omission could be, and in the circumstances would be likely to be, ratified by the company;

(e) whether the company has decided not to pursue the claim;
(f) whether the act or omission in respect of which the claim is brought gives rise to a cause of action that the member could pursue in his own right rather than on behalf of the company.

(4) In considering whether to give permission (or leave) the court shall have particular regard to any evidence before it as to the views of members of the company who have no personal interest, direct or indirect, in the matter.

In drafting a parallel article to Sec 263 allowing stakeholders to file a derivative lawsuit, there are a number of issues one could take into account.

First, it would be commendable to delete any language referring to the company's decision to authorise the directors' conduct. This reference is made to ensure that one shareholder would not be able to file a derivative suit on behalf of the company when the majority of the shareholders, or disinterested directors, approve the conduct of the board (Davies and Gower 2008: 617–621, Kershaw 2012: 606–628). This rationale would not be valid in a lawsuit brought by stakeholders, as they may have a different point of view from the one of the shareholders' body and may want to file a lawsuit despite the shareholders agreeing with the directors. This consideration, although intuitive, would, however, substantially modify the nature of the company's ownership and control. If stakeholders would be able to file a lawsuit on behalf of the company even against the will of both shareholders and directors, it would mean that the control of the company belongs to society, instead of the shareholders. This would represent, by itself, a revolutionary change in UK company law. However, Canada has already adopted a similar approach as shareholders' approval is not a determinative factor for courts to decide whether to allow stakeholders to file a derivative lawsuit (Ben-Ishai 2006).

Second, in order to avoid nuisance lawsuits filed by any person, one could imagine that only certain groups of stakeholders could be entitled to file such derivative lawsuits. This could include, for example, trade unions, consumer associations, NGOs, or a substantially large group of individuals that are affected by the activities of the company. Therefore, stakeholders that pursue a public or common interest would be entitled by law to file a derivative lawsuit on behalf of the company, while the others would not. This approach would also avoid the problem scholars have identified in Canada, where courts decide on a case by case basis who the proper person to file a derivative action is (Sarra 2006). In addition, one could also entitle to derivative lawsuits those groups or individuals that have a real interest in the company's conduct or have been impacted negatively by it. In this sense, the logic is opposite to the one currently adopted for shareholders. Sec 263 sets out that judges should have high regard for the evidence brought by those shareholders that have no interest in the matter. It also lists as one of the reasons to dismiss a lawsuit, the fact that a shareholder could pursue an action on its own. The purpose of these limitations is to avoid enabling a shareholder who has a personal interest in a matter to use the company to pursue an action that he could pursue on its own (Davies & Gower 2008: 617–21, Kershaw 2012: 606–28). In the case of stakeholders, however, one could accept an opposite logic, requiring an interest in the matter before pursuing it, in order to avoid nuisance lawsuits brought by a person who has no particular reason to sue the directors.

Third, should the derivative lawsuit be successful, any damage or reparation cost would belong to the company as the stakeholders would file a lawsuit on behalf of the company. This alone would be a strong disincentive for stakeholders to file nuisance lawsuits because they will not be able to benefit directly from such litigation. Moreover, this opens a number of questions in terms of the costs that such a lawsuit would have. A fundamental question in this regard is whether, subject to a court prima facie analysis of the claim, the company should bear the costs of lawsuits filed by stakeholders, who often have no means to litigate a case on their own behalf. This and other related questions should be taken into careful consideration in drafting a legislative proposal.

The oppression remedy

One of the reasons why shareholders rarely file derivative actions is that in a number of common law jurisdictions they can file an action on their own behalf against directors (Keay 2016). This action, defined as oppression remedy, substantially differs from derivative actions, for the following reasons.

First, the oppression remedy is a personal action that shareholders can use against directors that unfairly prejudice their interests (instead of the success of the company). This means that the interests of the shareholders and the one of the company may potentially diverge. For example, if directors act in the interest of the company but, by doing so, prejudice the interest of a shareholder, s/he can sue the board. Often majority shareholder(s) control the board and, therefore, it is for minority shareholder(s) to use the oppression remedy. Sometimes, the board breaches its duties of care and/or loyalty to the company and this also results in unfair prejudice to the shareholders. In this case, the derivative action and the oppression remedy may conflate, and a shareholder could sue the board on both grounds (Sarra 2006; Keay 2016).

Second, because it is a personal action both the costs and the prospective compensation arising from the lawsuit are due by/to the shareholders. The company is neither the claimant nor the receiver of any damages gained as a result of the litigation. It is, therefore, a remedy that would be typically preferred by shareholders vis-à-vis derivative actions because, if successful, they would directly benefit from the litigation (Davies & Gower 2008: 681–708; Kershaw 2012: 690–705; Keay 2016).

Third, while a derivative action can be initiated for breach of duties, given that the directors owe the duties of loyalty and care to the company, the oppression remedy can be used any time a mere interest of the shareholders is unfairly prejudiced (Sarra 2006).

In the UK, the Companies Act 1948 used to include the oppression remedy, which the Companies Act 2006 then re-framed as unfair prejudice remedy. In both Acts, the remedy is actionable by shareholders but not stakeholders (Davies & Gower 2008: 681–708; Kershaw 2012: 690–705).

The Canadian example

Canada entitles stakeholders with the oppression remedy. The Canada Business Corporation Act adopted one definition of stakeholders for both the derivative action and oppression remedy: any person considered as ‘proper’ at the discretion of the court.[14] However, the grounds to file oppression claims are more restrictive than those of derivative actions.

> Sec 241
> Grounds
>
> (2) If, on an application under subsection (1), the court is satisfied that in respect of a corporation or any of its affiliates
>
> (a) any act or omission of the corporation or any of its affiliates effects a result,
> (b) the business or affairs of the corporation or any of its affiliates are or have been carried on or conducted in a manner, or
> (c) the powers of the directors of the corporation or any of its affiliates are or have been exercised in a manner
>
> that is oppressive or unfairly prejudicial to or that unfairly disregards the interests of any security holder, creditor, director or officer, the court may make an order to rectify the matters complained of.

The Canadian judiciary clarified the meaning of such grounds and interpreted Sec 241 in a conservative way.

First, the oppression remedy at the common law has been developed for the benefit of minority shareholders and, therefore, in order to be a ‘proper person’ to file an oppression remedy a stakeholder must resemble a minority shareholder. Courts have validated such resemblance in cases of creditors in insolvency proceedings but have so far not admitted that employees could qualify (Sarra 2006).

Second, when a stakeholder uses the oppression remedy, it protects mere interests, which may conflate with the rights of shareholders. In this competition between stakeholders’ interests and shareholders’ rights, Canadian courts have often preferred shareholders’ rights (Ben-Ishai 2006; Sarra 2006).

Third, Canadian courts clarified that, differently from a derivative action, the oppression remedy is a personal action, which is not based on a breach of the duties of loyalty and care to the company, but rather on an unfair prejudice of the shareholders/stakeholders’ interests. Therefore, shareholders/stakeholders cannot sue the board for a breach of the duty of loyalty, because directors have no duty of loyalty towards either shareholders or stakeholders but only towards the company. Stakeholders/shareholders can instead file an oppression claim for breach of a duty of care which any person, including a director, could owe towards any other person, including a stakeholder or a shareholder (Vasudev 2015).[15]

[14] Canada Business Corporation Act Sec 238.

[15] See e.g. *BCE Inc. v. 1976 Debentureholders* 2008 SCC 69; *Royal Trust Corp. of Canada v. Hordo* (1993) 10 BLR (2d) 86 (SCJ); *Peoples Department Stores Inc. v. Wise* 2004 SCC 68.

Prospective oppression remedy for stakeholders in the UK

Given the Canadian approach allowing stakeholders to file oppression claims, a possibility for the UK legislator to enhance the accountability of the board could be to also adopt a stakeholders oppression remedy. A possible proposal in this direction would, however, trigger several important questions.

First, it would be commendable to define appropriately the class of stakeholders that can file an oppressive remedy, in order to avoid the reduction of such a class to creditors in insolvency proceedings. As already discussed for the derivative actions, such a class of stakeholders should arguably include trade unions, consumers associations, NGOs, or a substantially large group of individuals that are affected by the activities of the company.

Second, an oppression remedy would not be the proper remedy to enforce the duty of loyalty including the proposed amended Sec 172, because directors owe the duty of loyalty only to the company and not to shareholders or stakeholders. Therefore, a prospective oppression remedy could be used only in the circumstances in which the directors would violate a duty of care towards stakeholders detrimentally affected by the company's conduct.[16]

These considerations are not to say that a stakeholders' oppression remedy would be useless or not worth adopting. There are a number of arguments in favor of the adoption of a stakeholders' oppression remedy.

First, the oppression remedy would allow stakeholders to file lawsuits for breach of a duty of care against directors. This could be a powerful tool in terms of ensuring that the board does not harm stakeholders.

Second, any compensation arising from such a lawsuit would be for the stakeholders, instead than for the company. This would incentivise stakeholders to file lawsuits against directors but could also result in the filing of nuisance lawsuits against the board. It would be therefore commendable to set up a judicial check similar to the one established for derivative lawsuits.

Third, from a pluralistic corporate governance perspective, it may be arguable that if shareholders have the opportunity to file both derivative and unfair prejudice actions, stakeholders should as well be entitled to both remedies in order to ensure that the board would balance all interests at stake while managing the company. This would avoid the board preferring the shareholders' over the company's interests.

The drafting of a legislative proposal should take into account all of the above considerations.

[16] Although the distinction between duties owed to the company and interests of the shareholders is formally correct, note that UK courts have often received unfair prejudice claims for breach of duties. See Keay (2016).

Employees and the board

In a number of countries that do not follow the Anglo-Saxon legal tradition, director and workers cooperate in managing the company. This is a possible avenue to ensure that the board will make decisions not only in the interests of shareholders or its own, but also in the interests of employees. Various corporate models and legal systems include employees' participation in corporate governance. The most notorious example is co-determination, adopted by a number of countries following the German legal tradition of corporate governance. Similarly to Delaware, German company law embraces a pluralistic approach. The board must act in the company's interest, but such an interest is not defined in the law. Thus, directors are free to define the interest of the company as they see fit. Moreover, companies have a two-tier board (including a management and a supervisory board). The supervisory board elects and determines the pay of the management board. For public limited companies with more than 500 employees, either 30% or 50% (depending on the overall number of employees) of the supervisory board members must be employees representatives. This structure made scholars define Germany as a stakeholder value system because managers have no legal obligations to act in the interest of shareholders, in contrast to the English system, which instead requires directors to act for the benefit of shareholders. In addition, German managers have a considerable incentive (pay and appointment) to take into high consideration the interests of the employees alongside those of shareholders (Fauver & Fuerst 2006; Blair & Roe 2010; McGaughey 2015; Bottenberg *et al.* 2017; Rühmkorf 2019).

The German co-determination model is not the only one that allows employees to influence managerial decisions. For instance, in Japan, no law establishes a formal control of employees on the board. Nevertheless, the culture of Japanese boards is to regularly consult employees (either formally because they are part of a specific committee or informally). Moreover, directors are often senior employees that have worked in the firm for years. This is due to the historical role that employees play in Japanese industries, where they have life-long contracts of employment as well as several other benefits provided by employers (such as housing). In Japan, directors are typically insiders with little challenge to their authority. Nevertheless, the Japanese model can still be considered shareholder-oriented. Historically, Japanese firms were family-owned businesses, where the majority shareholder was the ultimate 'owner' of the company. The culture is such that shareholders, directors and employees are all committed to the company in the long term. However, with time, Japanese firms have increasingly opened to dispersed shareholder ownership and foreign investments. Thus, the traditional ownership and work structure (based on long-term commitment of shareholders, directors and workers to the company) exposed Japanese corporations to criticisms in terms of the respect of minority shareholders' rights (second agency problem), the competitiveness of Japanese enterprises in a global market, and a lack of supervision by independent directors. Therefore, in 2015, Japan started a series of reforms of its corporate governance system to make Japanese corporations more shareholders-oriented and encourage the introduction of independent board members. These reforms have also followed international trends to encourage companies to take sustainability and environmental concerns seriously. In this sense, Japan is an interesting example of a country attempting to combine a long-term and purposeful corporate culture with the demands of a globalised capital market (Jackson 2005; Jackson & Moerke 2005; Kozuka 2019; Seki 2019).

Whether or not involving employees in corporate management is efficient is part of a complex debate that academics and the business community have engaged in for decades and which is not for this article to repeat. Nevertheless, no matter the view one could adopt, co-determination or similar models could represent a possible avenue for at least some stakeholders to exercise a certain level of control over the board. This could be, however, a sub-optimal solution because it would allow only employees to take part in the life of the enterprise, while excluding other stakeholders, such as communities affected by the industrial activities or NGOs representing environmental concerns.

In 2018, the newly revised Corporate Governance Code has taken the question of stakeholders on the board into account by introducing Principle 1E) and Provisions 5 and 6.

> Principle 1 E): Board Leadership and Company Purpose
>
> The board should ensure that workforce policies and practices are consistent with the company's values and support its long-term sustainable success. The workforce should be able to raise any matters of concern.
>
> Provision 5:
>
> The board should understand the views of the company's other key stakeholders and describe in the annual report how their interests and the matters set out in section 172 of the Companies Act 2006 have been considered in board discussions and decision-making. The board should keep engagement mechanisms under review so that they remain effective.
>
> For engagement with the workforce, one or a combination of the following methods should be used:
>
> - a director appointed from the workforce;
> - a formal workforce advisory panel;
> - a designated non-executive director.
>
> If the board has not chosen one or more of these methods, it should explain what alternative arrangements are in place and why it considers that they are effective.

Provision 6:

> There should be a means for the workforce to raise concerns in confidence and –if they wish– anonymously. The board should routinely review this and the reports arising from its operation. It should ensure that arrangements are in place for the proportionate and independent investigation of such matters and follow-up action.

First, it is important to recall that the Corporate Governance Code is a comply or explain set of principles which applies to companies with a Premium Listing of equity shares. It aims at providing guidance, rather than prescribing a conduct for companies. Furthermore, given the current structure of UK company law being a shareholders primacy jurisdiction, any change in the way the directors manage the company is currently subjected to the shareholders' approval and control. This includes also the possibility for directors to engage with stakeholders.

Second, although Provision 5 refers to the engagement with stakeholders other than the workforce, it is unclear how such an engagement should happen. While as to the workforce there is an indication that it should participate in the management of the company (through either a designated non-executive director, an advisory panel, or a member of the board appointed by workers); as it pertains to other stakeholders there is no recommendation as to how the board should engage with them. A number of avenues could be explored. Certainly, the possibility to have only one member of the board coming from the workforce, would not be enough to represent the wide variety of stakeholders' interests. One could imagine an advisory panel including not only employees, but other stakeholders, or the introduction of a supervisory board with representatives from a wide variety of stakeholders.

Scholars that have analysed whether co-determination could help companies become more socially responsible have raised two main concerns. First, how stakeholders' participation should happen on a global scale. For instance, if a UK company is the head of a corporate group making clothes in India, the employees and the communities affected by such activities would likely be in India. Certainly, the decision of the board in London would have a direct effect on the lives of stakeholders in India. It would make, therefore, sense to consider in which capacity these people could contribute to the governance of the corporate group. For instance, how would an advisory panel reflect the interests of those stakeholders affected by the group? Second, the interests of employees may not necessarily be aligned with that of the environment or other stakeholders affected by the activities of corporations. Like shareholders, also stakeholders are a diverse group including people that have sometimes divergent interests (Kozuka, 2019; Rühmkorf, 2019; Gelter, 2016).

A legislative reform should take all of these considerations into careful account in order to ensure that various interests are represented in the board of directors.

The accountability approach: externalising stakeholders' interests

A different avenue to enforce the proposed new draft of Sec 172 could be to hold the company to account when stakeholders are detrimentally affected by its activities. This avenue transforms the concerns of stakeholders as external liabilities for the company. Stakeholders would not exercise control over the board. However, the board would have to take their concerns into account to avoid liabilities for the company. There are various sanctioning mechanisms that one could implement to enforce stakeholders' rights against a multinational company. This article will briefly analyse two mechanisms that have become increasingly relevant in a number of jurisdictions. The first one is to introduce reporting obligations and corresponding penalties for companies that do not comply with certain standards; the second one is to allow stakeholders to file civil liability complaints against parent companies for the extraterritorial conduct of their foreign subsidiaries or supply chains.

Reporting obligations and penalties

The proposed changes of Sec 172 could be strengthened by some reporting obligations and corresponding penalties for those companies that do not fulfil their purposes.

This approach, introducing reporting obligations, is not new. For instance, the UK Modern Slavery Act requires holding companies to report on modern slavery and human trafficking within their supply chains[17] (Fasciglione 2016). The Corporate Governance Code itself prescribes companies to report as to whether or not they comply with it. Most specifically, according to Provision 5 (see above) the board should report on the way it took into account the interests of stakeholders in its decision-making. However, such laws have not established penalties for companies that fail to comply with the suggested best practices. For this reason, scholars often criticise reporting obligations as they do not ensure proper enforcement of the conduct they prescribe (Broad & Turnbull 2018; North 2018).

Against this background, some states have recently combined reporting obligations with sanction mechanisms. In 2019, the Netherlands adopted a piece of legislation, the Child Labour Due Diligence Law. The law establishes a due diligence obligation for companies consistently selling their products in the Netherlands (including both Dutch and foreign companies) to prevent child labour across their supply chain, in connection with reporting obligations. It is one of the first examples of a sanctioning regime applicable to companies that fail to comply with due diligence and reporting obligations. It appoints a regulator to receive complaints from victims and to assess

[17] *Modern Slavery Act 2015*: chap. 30, part 6, s. 54 Transparency in supply chains etc.

the due diligence plan companies put in place and/or the accuracy of their reports. The sanctions include fines on the company and criminal liability on the directors (Hoff 2019).[18]

Germany also adopted a similar law, the Supply Chain Due Diligence Act. In comparison with the Dutch law, the German law applies only to companies incorporated in Germany (and not to foreign companies targeting the German market), but it is wider in scope because it refers to the responsibility of German companies for all human rights abuses (and not only child labour) committed by their subsidiaries and direct suppliers. Similar to the Dutch law, the German law enables a federal authority, the Federal Office for Economic Affairs and Export Control, to sanction companies in breach of their due diligence obligations and to hear complaints from victims.[19]

Against this background, one could imagine introducing a similar penalty regime for companies that fail to meet their reporting obligations in connection with an authority that is able to hear victims' complaints and assess the reports filed by companies.

This could be achieved by changing Secs 9-16 of the Companies Act to ensure that companies registered in the UK would:

1) State their purposes at the time of incorporation;
2) Publicly report on the positive and negative externalities of such purposes on an annual basis;
3) If a company owns a subsidiary, it must also state the purposes of the corporate group and report on such purposes.

The law should also introduce a set of penalties and fines for those companies that do not comply with their purposes.

First, the Registrar of Companies would have to check that the purposes of the company have been appropriately defined, taking into fair regard various interests and not only the one of the shareholders. If the company does not appropriately define its purposes, the registrar could refuse to register it in the UK.

Second, the company would have to publicly report on the positive and negative externalities of such purposes, in order to increase the public pressure on companies to pursue their purposes.

[18] Wet van 24 oktober 2019 houdende de invoering van een zorgplicht ter voorkoming van de levering van goederen en diensten die met behulp van kinderarbeid tot stand zijn gekomen (Wet zorgplicht kinderarbeid) 2019.
[19] Gesetz über die unternehmerischen Sorgfaltspflichten in Lieferketten 2021 2959.

Finally, if a company does not pursue its purposes, it should be penalised. One could imagine an authority, such as the Financial Conduct Authority, to be in charge of reading the reports filed by companies and overseeing whether their conduct meet their purposes. Such an authority could also receive stakeholders' complaints in order to get informed as to the negative externalities of companies.

This approach would be in continuity with already existing reporting obligations but would make such obligations more effective by introducing sanctions for companies that fail to comply.

Liability in tort law

A possibility to prevent multinational enterprises from harming others is to hold parent companies accountable when the group damages third parties. This is a possibility that has been explored by litigators in various jurisdictions.

In common law jurisdictions, and specifically in the US, the UK and Canada, litigators have increasingly argued for a progressive interpretation of tort laws in order to hold parent companies accountable for negligence resulting in their foreign subsidiaries damaging stakeholders. For instance, in the US, litigators have interpreted in a progressive way the Alien Tort Statute, a piece of legislation connecting common law causes of actions in tort with violations of the Law of Nations (which could be interpreted as international law) (Enneking 2008; Giannini *et al.* 2011). This approach is now of limited application after two decisions of the US Supreme Court.[20] In Canada, litigators have been more successful in following a similar path. They combined causes of actions in torts with alleged violations of international law committed by multinational enterprises to file suits in Canadian courts.[21] UK litigators have instead pioneered a different approach focused on the concept of a duty of care in tort law and without referring to human rights and international law. This strategy seems increasingly successful after the recent UK Supreme Court decisions *Lungowe v Vedanta* and *Okpabi v Shell*, which allow UK courts to assert jurisdiction over UK parent companies for the alleged breaches of their duty of care in respect of the torts committed by their foreign subsidiaries.[22]

[20] *Kiobel v Royal Dutch Petroleum Co* [2013] US Supreme Court 133 S. Ct. 1659; *Jesner v Arab Bank, PLC* [2018] US Supreme Court 584.

[21] *Nevsun Resources Ltd v Araya* [2020] Supreme Court of Canada.

[22] *Vedanta Resources PLC and another (Appellants) v Lungowe and others (Respondents)* [2019] UKSC 20; *Okpabi & Ors v Royal Dutch Shell Plc & Anor* [2021] UKSC 3.

A different approach has been to adopt mandatory due diligence laws that would require companies incorporated in a certain jurisdiction to oversee the activities of their affiliates worldwide. In case of breach of such obligation, the holding company would be accountable for the damages suffered by third parties.

France passed the first law ever to establish an extraterritorial due diligence obligation for French companies with over 5,000 or over 10,000 employees (depending on whether the corporate group includes only French or also foreign companies) to set up a monitoring plan overseeing the activities of its corporate groups worldwide. The monitoring plan shall prevent threats to human rights, environment, health or security. The parent company's monitoring obligation includes both subsidiaries and companies with which it has an established commercial relationship (supply chain). This obligation is connected to a tort law cause of action that allows victims to file a complaint against French parent companies. The burden of proof on the victim is, however, high: a victim has to prove, first, that the affiliate violated human rights, environmental standards or laws protecting health or security; second, that the parent company violated its due diligence obligation (i.e. it did not set up a monitoring plan); third, that the affiliate would not have violated such laws if the parent company fulfilled its due diligence obligation; and, finally, that such abuses resulted in damage (Périn Pierre-Louis 2015; Cuzacq 2016; Cossart *et al.* 2017; Pataut 2017).[23]

The European Union is attempting to introduce a similar, but more advanced, piece of legislation on mandatory human rights and environmental due diligence. The European Parliament and Commission proposed two versions of a directive that would establish obligations for states to set up mandatory human rights and environmental due diligence laws applicable to several companies incorporated in the European Union, and, under some circumstances, to foreign companies accessing the European market. Moreover, the proposed directive introduces strong enforcement mechanisms. It would require states to establish, on the one hand, competent authorities sanctioning companies in breach of their due diligence obligations, and on the other hand, civil liability remedies entitling victims to file suits against companies for violations of their due diligence obligations.[24]

[23] *Loi 2017-399 du 27 mars 2017 relative au devoir de vigilance des sociétés mères et des entreprises donneuses d'ordre* 2017.

[24] European Commission, Directive of the European Parliament and of the Council on Corporate Sustainability Due Diligence and amending Directive (EU) 2019/1937 COM (2022) 71 final; European Parliament resolution of 10 March 2021 with recommendations to the Commission on corporate due diligence and corporate accountability 2021 (2020/2129(INL)).

Against this background, the Joint Committee on Human Rights of the UK Parliament also called in 2017 for the Government to adopt a due diligence obligation law.[25] A possibility, to ensure the accountability of UK corporations, could be to draft a proposal for a mandatory due diligence law, taking into account two elements: the harm such a law should prevent and the liability regime that it should impose on corporate groups.

Harm

In order to draft such a law, one of the fundamental questions to address would be what kind of harm should a corporate group prevent? The answer to this question is not straightforward as there are different levels of harm one could take into account going from gross human rights abuses to any monetary damage inflicted on third parties.

In this regard, it could be of help to consider an old proposal rejected by the UK Parliament in 2002 for a Corporate Responsibility Bill. According to Section 6:

> (1) A parent company of a corporate group shall be liable to pay compensation in respect of the classes of damage set out in subsections (1)(c)(i) to (iii) below where—
>
> (a) the manner in which the group's activities are organised managed or undertaken falls below the standards that can reasonably be expected of the group in all the circumstances of the given case; and
> (b) *the manner in which the group's activities are organised managed or undertaken fails to ensure—(i) the health and safety of persons working in or affected by those activities; (ii) the protection of the environment; and*
> (c) *such a failure may be regarded as a cause of—(i) serious physical or mental injury to persons working in or affected by those activities; (ii) serious harm to the environment; or (iii) both.*
>
> (2) For the purposes of this section it shall be immaterial whether the injury to persons or harm to the environment occurred within the United Kingdom.
> (3) It shall be the duty of a company to which subsection (1)(a) applies to ensure that—(a) any other entity which is under that company's operational control wherever registered or domiciled complies with sections 3, 4, 5, 7 and this section; and (b) any subsidiary undertaking of that company wherever located complies with sections 3, 4 and 5.[26]

[25] Joint Committee on Human Rights UK Parliament, '6th Report - Human Rights and Business 2017: Promoting Responsibility and Ensuring Accountability - Joint Committee on Human Rights - House of Commons' (2017) HL Paper 153, HC 443 <https://publications.parliament.uk/pa/jt201617/jtselect/jtrights/443/44302.htm> accessed 21 January 2019.
[26] *Corporate Responsibility Bill*, 2002, sec. 6.

Sections (b) and (c) of the Corporate Responsibility Bill established the harm that corporations should be liable for. It included the failure to ensure the health and safety of workers or the protection of the environment in combination with a serious injury to person or harm to the environment. This is quite a limited list of harms and injuries which would, however, cover the most outrageous abuses. It is also a list of harms which does not refer to any internationally recognised standard such as human rights or environmental laws. By contrast, the French law refers to *any serious threat to human or environmental rights, health or security.* The European Union proposals for a directive echo a similar language. Both include a wider range of harms than the Corporate Responsibility Bill, affecting not only workers or the environment, but also, for example, human rights defenders abused by corporations.[27]

A drafting committee would have to consider these different approaches to define what level of harm a future law should prevent.

Liability

As mentioned above, UK courts have already developed quite complex jurisprudence on the parent company's liability for the damages committed by its subsidiaries. This caselaw is based on the parent company's breach of a duty of care owed to victims for the activities of its corporate group. It would, therefore, be commendable to develop a liability regime on the basis of such an established concept of the duty of care.

Essentially, under UK tort law, a parent company could potentially owe a duty of care towards third parties affected by the activities conducted by its subsidiaries (Enneking 2012; Sanger 2012; Baughen 2013; Petrin 2013; Palombo 2015; Roorda & Leader 2021). The question UK courts have left unanswered is under which circumstances would such duty of care be established. It is complicated to provide an answer as UK courts have delivered various cases on the duty of care but have only recently applied such concepts to parental liability in corporate groups. For the moment, there are three particularly significant cases: *Chandler v Cape plc*, a case recognising the existence of a parent company's duty of care for the damages committed by its

[27] European Parliament resolution of 10 March 2021 with recommendations to the Commission on corporate due diligence and corporate accountability 2021 (2020/2129(INL)); Loi 2017-399 du 27 mars 2017 relative au devoir de vigilance des sociétés mères et des entreprises donneuses d'ordre 2017 (JORF); European Commission, Directive of the European Parliament and of the Council on Corporate Sustainability Due Diligence and amending Directive (EU) 2019/1937 COM (2022) 71 final.

subsidiaries;[28] and the Supreme Court cases *Lungowe v Vedanta* and *Okpabi v Shell*.[29] However, *Chandler v Cape plc* is a purely domestic case. *Lungowe v Vedanta* and *Okpabi v Shell* promisingly recognise that the duty of care jurisprudence may apply to multinational enterprises, but these are cases decided on the issue of jurisdiction only. Some recent cases,[30] potentially open the door for UK companies to owe a duty of care in respect of not only the activities of their subsidiaries, but also of their suppliers, but it is still early to understand how the duty of care jurisprudence would apply in this context. It is therefore unclear under which circumstances and conditions a parent company would owe a duty of care towards third parties for the damages committed by its subsidiary/supplier.

Thus, it would be commendable for a mandatory due diligence law to detail the conditions under which a parent company owes a duty of care towards third parties for the harm committed by its subsidiaries. Specifically, the committee drafting a legislative proposal could take into consideration the following question: what shall the relationship be between a parent company, a subsidiary or supplier and a victim for the parent to owe a duty of care towards the victim?

Assessment

The Purpose and the Do No Harm Objectives are fundamental goals for future corporations. The legal framework should regulate the conduct of corporations having such two goals in mind.

The Purpose Objective is achievable by modifying Sec 172 and re-focusing UK company law to follow a pluralistic, rather than a shareholders primacy, approach. This change seems achievable and not far away from the experience of other countries where corporate governance follows a pluralistic approach, not focused on the sole interests of the shareholders. While this approach would open the doors to entrepreneurs that are interested in offering profitable solutions to the problems of people or planet, it would not be sufficient to ensure that those companies that have a narrow focus on profit do not harm third parties.

The Do No Harm Objective is achievable only by establishing enforcement mechanisms that would ensure the accountability of the board and/or the company

[28] *Chandler v Cape Plc* [2012] (QB), X (appeal taken from Eng) EWCA civ 525.
[29] *Vedanta Resources PLC and another (Appellants) v Lungowe and others (Respondents)* [2019] UKSC 20; *Okpabi & Ors v Royal Dutch Shell Plc & Anor* [2021] UKSC 3.
[30] See e.g. *Begum v Maran (UK) Ltd* [2021] EWCA Civ 326.

when stakeholders are negatively impacted by its activities. There are a variety of approaches that one could take in order to ensure enforcement.

A first avenue, that one could label as *control*, would be to allow stakeholders to exercise some control over the directors. This could be achieved either by allowing stakeholders, like shareholders, to elect directors (co-determination), or by allowing stakeholders, like shareholders, to sue directors (derivative lawsuits and/or oppression remedy).

There are a number of jurisdictions that have already experienced co-determination, even if in such models the stakeholders participating in the board are typically employees and/or trade union representatives. The recent Corporate Governance Code has also taken an approach moving towards this direction.

The derivative and oppression remedy approach has also been implemented by a few jurisdictions, such as Canada. However, there is no country which established a mechanism specifically designed for stakeholders to file actions against the board. Such a mechanism could create a preferred litigation route for those stakeholders that represent the interest of numerous people or a significant public interest, such as NGOs representing environmental concerns or trade unions representing employees.

A second avenue, that one could label as *accountability*, would be instead to allow stakeholders to file complaints against multinational enterprises. This could be achieved by either establishing new mandatory obligations for parent companies in connection with civil liability, or, in the alternative, by penalising companies that do not take into proper consideration the interests of stakeholders.

France adopted a mandatory due diligence law. The European Parliament and Commission have already proposed two versions of a possible directive. The Joint Committee on Human Rights of the UK Parliament also suggested a similar approach and the UK Supreme Court opened the door to tort claims filed against parent companies in connection to extraterritorial harms. It seems that this legislative reform could represent a reasonable step forward for the UK legislator.

The two avenues of *control* and *accountability* present different challenges.

The *control* avenue internalises the problems that stakeholders face within the companies by providing them a certain level of control over the board. Such internalisation process has the advantage to combine the Purpose and the Do No Harm Objectives because the impact that stakeholders would have on the board could help both in terms of companies providing profitable solutions for people or planet, and in terms of ensuring that businesses do no harm to others.

However, the level of accountability that such a solution would entail is dubious. For example, if only one member of the board would represent stakeholders, its power would be limited as it could always be outnumbered by the other directors. Also, if derivative actions by stakeholders would be allowed only in relation to purposes entirely defined by the shareholders, then the impact of these lawsuits would also be limited. Imagine, for example, a company defining its purpose as ‘to find profitable solutions for our clients worldwide’. Such a purpose would address both shareholders’ and customers’ interests, but it would say nothing about the environment. A community affected by environmental degradation committed by the company would unlikely be able to sue the directors for breach of duties, even if allowed to file a derivative lawsuit, because such legal action could be brought only in connection with the directors’ failure to promote a purpose drafted in the shareholders’ interest. The oppression remedy could fill this gap, but it would have to clarify what class of stakeholders and interests should be detrimentally affected in order to file an oppression claim. Therefore, the *control* route may not necessarily achieve the Do No Harm Objective.

The *accountability* avenue externalises the problems stakeholders have by providing them with a route to sanction businesses that detrimentally affect them. The externalisation process has the advantage of setting up a benchmark as to the companies conduct (being either an administrative authority or the stakeholders affected by the activities of businesses). Such an external benchmark could arguably ensure a higher level of accountability, and therefore better fulfil the Do No Harm Objective.

However, this approach does not incorporate the Purpose Objective. First, stakeholders would not impact the board’s decisions directly as directors would not be accountable to them. Nevertheless, the fact that they could sue the company may have an indirect impact on the board’s conduct, which would take the threat of possible lawsuits into consideration when managing the company. Second, even if the lawsuits brought by stakeholders would have an impact on the board’s decision-making, this would be limited to the board avoiding possible liabilities for the company, rather than managing the company to positively impact society. Arguably, for the board to find solutions for people or planet, stakeholders should be members of the board, or able to hold the board to account, or both. Nevertheless, the failure to incorporate the Purpose Objective may not represent such a problem, if the Purpose Objective would be already achieved by the proposed changes of Sec 172. In this case, Sec 172 would aim at Purpose, while the *accountability* approach would focus on achieving Do No Harm.

The UK legislator could also opt for a synthesis between these legislative proposals, combining, on the one hand, the ability for stakeholders to control the board, and on the other, the accountability of multinational enterprises for extraterritorial damages.

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Acknowledgments

I would like to thank Colin Mayer, Daniela Weber Rey, Claire Russell, Luke Fletcher, David Kershaw, Daniel Leader, Bill Clark, all of the contributors to the Future of the Corporation programme, and the anonymous reviewer for their extremely useful insights. However, please note that the views of the author are her own. Note that parts of this article are also included in: Palombo, D. (2019), 'The Duty of Care of the Parent Company: A Comparison between French Law, UK Precedents and the Swiss Proposals', *Business and Human Rights Journal*, 1; Palombo, D. (2020), *Business and Human Rights: The Obligations of the European Home States* (Hart Publishing).

To cite the article: Palombo, D. (2022), 'The Future of the Corporation: the avenues for legal change', *Journal of the British Academy*, 10(s5): 43–86. https://doi.org/10.5871/jba/010s5.043

Journal of the British Academy (ISSN 2052–7217) is published by
The British Academy, 10–11 Carlton House Terrace, London, SW1Y 5AH
www.thebritishacademy.ac.uk

Journal of the British Academy, **10(s5)**, 87–123
https://doi.org/10.5871/jba/0010s5.087
Posted 26 August 2022

Through the looking glass: tying performance and materiality to corporate purpose

J.C. Stroehle, K. Soonawalla and M. Metzner

Abstract: By making use of the purpose definition set out by the British Academy's Future of the Corporation programme we argue that performance relates to purpose in two dimensions. Firstly, purpose sets the frame of long-term success and defines materiality for an organisation both from a single and from a double materiality perspective. Secondly, performance in relation to purpose needs to measure profitability net of negative externalities. We review and discuss the current landscape of non-financial reporting and measurement frameworks on how they lend themselves to the determination of materiality on the one hand and to the accounting of externalities on the other hand, in order to achieve an approximation of performance in relation to purpose. We conclude by discussing how materiality and measurement viewed through a purpose-lens could help an advanced understanding of performance in practice for sustainable finance, corporate governance and management decision-making.

Keywords: Non-financial measurement and performance, materiality, corporate purpose, sustainability accounting.

Note on the authors: see end of article.

Introduction

Friedman's (1970) doctrine of shareholder primacy is increasingly being challenged, in business, society, and capital markets. These changes are attributed in part to market shocks, such as the financial crisis, and to the gravity and urgency of systemic 'wicked' challenges, such as climate change and income inequality. To cope with this, companies are expected to redirect their focus from maximising shareholder value to a vision of corporate purpose that allows them to focus on providing 'profitable solutions for people and planet, without profiting from the creation of harm' (British Academy 2019; Mayer 2018). This poses a challenge to companies, as the financial markets of the past half century have created a corporate focus vastly different from this vision. While annual financial reports, accounting standards and stock prices are intended to track and report a company's financial health, they are very limited in capturing information about the non-financial performance and intangible value of a firm. In other words, if corporate purpose was to become a template for the corporation of the future, current performance measurement would be largely unfit.

Recent trends in corporate reporting and investment practice seek to address the concern that current performance measurement is not holistic enough. At company level, increased stakeholder pressure and a growing realisation of the linkages between long-term liabilities and system level challenges are pushing boardrooms to engage in conversations beyond traditional financial profit (Gordon 2018; Enacting Purpose Initiative 2020; 2021). In recognition of these multiple objectives and concerns, and to construct a sustainable strategy, many companies have begun to address and manage the scarcity and vulnerability of intangible and non-financial assets, such as workers, communities, and natural resources through a variety of disclosure mechanisms and so-called 'full cost accounting' systems (Bebbington *et al.* 2007; Unerman *et al.* 2018; Stroehle & Rama Murthy 2019). In parallel, the incorporation of environmental, social and governance (ESG) factors into investment decisions has become important to institutional investors. What used to be a niche strategy, often driven by ethical values, has increasingly gone mainstream under the recognition that environmental and social dependencies are important risk-factors which should be priced into the construction of investment portfolios (Eccles *et al.* 2014; Khan *et al.* 2016; Beal *et al.* 2017).

Yet, despite the heightened awareness and practice around sustainability measurement and reporting, performance in relation to corporate purpose remains elusive. This is in part because there are no universally agreed-upon or mandated set of non-financial measures; companies and investors must choose from a wide variety of methodologies and definitions offered by a complex ecosystem of international organisations, non-governmental organisations (NGOs) and commercial data vendors. It also relates to the fact that purpose and performance are seldom thought about in conjunction: the one being a broad strategic goal of why the company exists, the other relating to a set system of (mostly financial) metrics and objectives.

Making use of the definition of purpose set out by the British Academy's 'Future of the Corporation' programme, we outline how performance relates to purpose in two dimensions. Firstly, purpose sets the frame of long-term success and defines materiality for an organisation. It is therefore important for determining which non-financial key performance indicators (KPIs) are material to assess the social or environmental problem that a company addresses, and to measure the outcomes and impacts associated with the activities it is pursuing in addressing this problem. Secondly, performance in relation to purpose should measure profitability net of negative externalities.[1] To achieve this, both a view of financial performance of a given product or service, as well as an assessment of the negative externalities associated with a product or service are important. A business solution in relation to purpose is therefore only profitable if it can absorb the costs associated with maintaining or rebuilding depleted social and natural capital and remedying harm done in the process of providing business solutions.

Following this logic, the paper is structured as follows. In the next section, we discuss materiality in relation to purpose and how it influences the choice of non-financial performance measures. Section 3 reviews the current landscape of measurement and reporting frameworks as well as current efforts of standardisation, discussing whether and how these aid performance measurement in relation to purpose. Section 4 discusses how to apply measurements to purpose in three core areas and reviews how notions of purpose can be included in the financial accounts. We highlight the challenges of this and show how different management accounting methodologies address and approximate a notion of profit net of harm through full-cost accounting and impact valuation. Finally, we discuss the utility of non-financial measurement in different areas, outlining the limits in current practice and discussing how a stronger tie to purpose could be useful. We draw on nine expert interviews, four examples of corporate practice and three focus groups of British Academy workshops to inform our reading of the current measurement landscape.[2] Section 5 summarises and concludes.

[1] The concept of externalities originates from economics and describes the positive and negative effects of market transactions on third parties that are not reflected in market prices.

[2] Details of the interviews and case studies are in Appendix 1 and Appendix 2.

Measuring corporate purpose

Non-financial measures tend to approximate sustainability-related performance and risk by looking at environmental, societal and governance aspects of a firm. In the absence of standards, a wide range of services and frameworks have been developed which propose measurement methodologies and reporting guidelines for companies to define their non-financial performance. In parallel, external ESG evaluations (rankings, indices, etc.) for investors are plentiful, making use of proprietary methodologies for their assessments (Eccles & Stroehle 2018). These developments have led to a confusing universe of choices for companies seeking to measure performance in the context of purpose. In this section we reflect on purpose through the lens of materiality to navigate this universe. In financial reporting, 'Information is material if omitting, misstating or obscuring it could reasonably be expected to influence decisions that the primary users of general purpose financial statements make on the basis of those financial statements, which provide financial information about a specific reporting entity.'[3] Further to this, materiality in relation to sustainability offers organisations lenses for determining the environmental, social and governance issues that are most important to them. Existing frameworks of reporting and advances towards a standard in non-financial reporting cater to different materiality lenses, and we discuss whether and how they can be helpful in supporting a view of performance in relation to purpose.

Purpose-led measurement and materiality

Since the notion of corporate purpose focusses on providing profitable solutions to the problems of people and planet, it stands to reason that performance in relation to purpose then needs to measure the attainment of said solution. The selection of non-financial KPIs is hereby key for a company to know whether it has achieved its purpose. Since not all non-financial issues are relevant to solving a given problem, the company needs to go through a process of reflection and select a set of indicators best suited for articulating the alignment with its purpose. This is where materiality comes into play. When defining materiality in the context of purpose, companies need to know their organisational, operational, and wider boundaries and the stakeholders associated with them. While the traditional boundary of the firm is tied to notions of ownership and control, a purpose-driven company would, by nature of what it is interested in, apply broader criteria which allow an assessment of its externalities,

[3] IASB, Conceptual Framework for Financial Reporting (2018), https://www.ifrs.org/news-and-events/news/2018/10/iasb-clarifies-its-definition-of-material/

i.e., the environmental and social consequences of its business activities for third parties.

If a company looks beyond traditional firm boundaries, it can consider the importance of externalities in two ways (see Figure 1). Firstly, the firm can recognise the importance of people and planet for its sustained financial success. This is often called 'financial materiality' or 'single materiality' and focuses on the impact that environmental and social factors have on the financial performance of a firm. These are particularly important factors from an investor perspective, and much of ESG measurement tries to approximate whether and how firms manage environmental and social risks and opportunities appropriately. Secondly, the firm can recognise the impact of its activities for people and planet beyond the financial perspective. This is also called the impact-perspective or 'double materiality', where companies seek to gain an understanding of how their operations and products affect social and environmental factors within and beyond their organisational and operational boundaries. The resulting information is of particular interest to stakeholders such as policymakers and civil society.

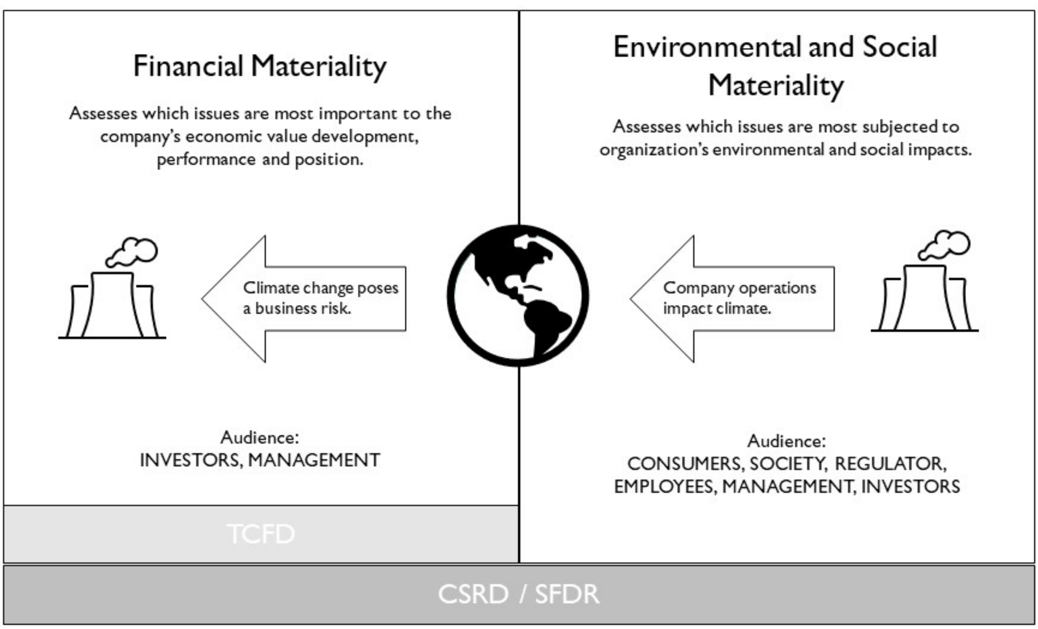

Figure 1. Single and double materiality. Note: figure adapted from the EU Commission's Climate-related information reporting guidelines, 2019, p. 7 (https://ec.europa.eu/finance/docs/policy/190618-climate-related-information-reporting-guidelines_en.pdf). Abbreviations refer to the Task-force for climate-related financial disclosure (TCFD), the European Commission's Corporate Sustainability Reporting Directive (CSRD), and the Sustainable Finance Disclosure Directive (SFDR).

The chosen materiality lens has direct consequences for non-financial measurement. Performance measurement related to organisational and operational boundaries consider corporate action (inputs) and the direct outputs created (such as production, scope of distribution). They provide a shareholder-centric view. Performance measures related to interest beyond the boundary of the firm, on the other hand, also focus on outcomes (changes in the natural and social environment) and impacts (consequences of these changes, such as environmental degradation, social unrest due to resource scarcity, etc.) of corporate activities. This allows an impact-oriented view that considers a wider group of stakeholders, of which shareholders are only one.

The notions of single and double materiality are not mutually exclusive and are widely recognised as interdependent or even nested (Impact Management Project [IMP], 2020) since a firm's management of its externalities will inadvertently impact the environmental and social risks it is exposed to. Climate change, for example, has traditionally been seen as being within the realm of double materiality, i.e., as a consequence of corporate activities. However, as more is known about physical and transition risks, and as it becomes a priority in the public debate, climate change is now widely recognised as a financial risk to business. The creation of emission trading systems and carbon prices are an institutionalisation of this recognition, and frameworks such as the Taskforce for Climate-Related Financial Disclosures (TCFD) have emerged to capture and formulate the single materiality lens of climate change.

Still, because the two concepts essentially cater to different interests regarding the information they provide, single and double materiality are often used in polemic debates around extreme standpoints. Recently, NGOs have also brought up new notions of context-related materiality into the discussion which tries to highlight the local dependency of materiality. From a purpose perspective, the discussion about whether single or double materiality is superior actually misses the point. If materiality is to inform purpose it is not an either/or logic that applies but a both/and one. We map the different logics of materiality to the different elements of corporate purpose to argue that a company needs to consider both perspectives in order to meaningfully measure performance in relation to purpose. We argue that any definition of performance in context of corporate purpose would require non-financial measurements utilised in corporate accounting and reporting to combine both shareholder and stakeholder orientations. The former is necessary to assess whether companies' actions are profitable, and the latter is required for evaluating if interventions indeed solve the problems of people and planet. In other words, when looking through the lens of purpose, single and double materiality are inextricably linked. Figure 2 illustrates this mapping.

Consistent with this mapping, Barker (2019) suggests: 'More effective, from a natural capital perspective, would be to link corporate reporting on environmental impact to science-based social targets, aligned for example with the UN's Sustainable

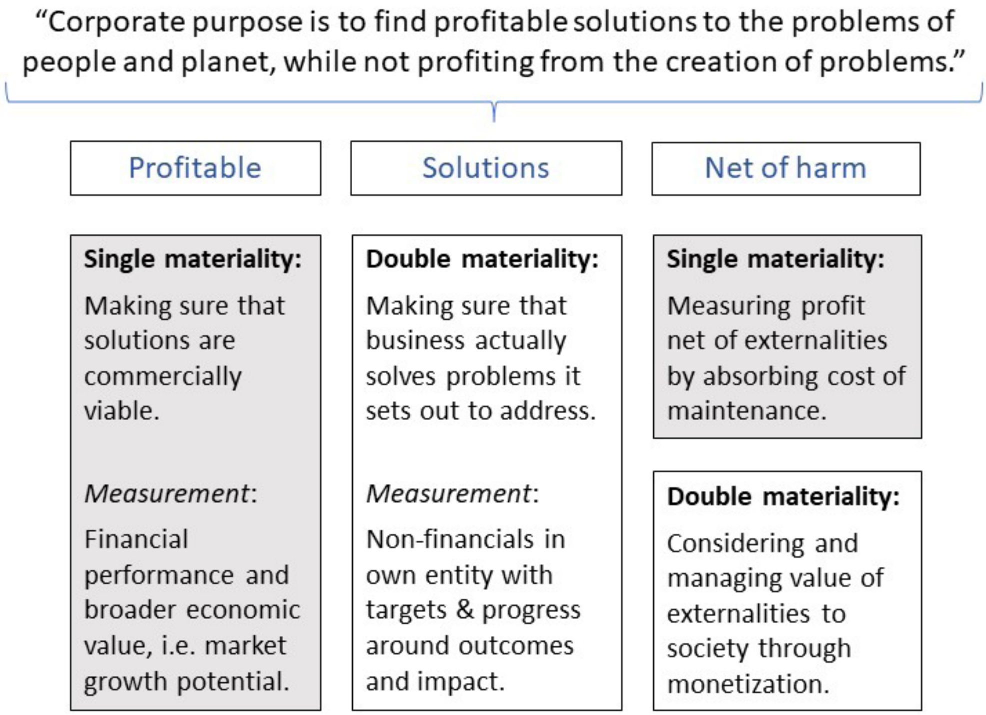

Figure 2. Materiality through the purpose lens.

Development Goals (SDGs). And yet this would imply a stakeholder orientation, which runs against the direction of travel of corporate reporting frameworks and practice.' We argue it is only the combination of both that allows a holistic perspective.

Frameworks for non-financial disclosure and materiality

To date a number of frameworks and guidelines exist to aid in the disclosure of non-financial information. A selection of some of the most important frameworks and standard setters in the non-financial reporting sphere are summarised in Table 1. These are categorised into principles of practice, conceptual frameworks, and data standards.

Principle of practice frameworks generally outline broad principles which describe good practice and processes of due diligence that organisations should adopt if they want to be responsible and long-term focussed. Work done by the IMP[4] suggests that the broad understanding of what defines a sustainable and diligent process is relatively

[4] These insights were gained through interviews held for this British Academy project. Publication with their evidence is said to be forthcoming.

Table 1. Selected institutions and frameworks for the measurement and management of non-financial information.

Institution / Framework	*Acronym (Type, Foundation)*	*Actors directed at*	*Description*	*Materiality-lens*
Standards of Process and Practice				
United Nations, Sustainable Development Goals	UN SDGs (Intern. Org., 2016)	All	A set of global goals as “blueprint” to create a more sustainable future. Successors of the Millennium Development Goals, the seventeen Goals are set to be achieved by 2030.	Double Materiality
The Organisation for Economic Co-operation and Development, Guidelines for Multinational Enterprises	OECD Guidelines (Intern. Org., 2004)	Governments	The Guidelines are a set of recommendations on responsible business conduct addressed by governments to MNEs operating in or from adhering countries.	Double Materiality
United Nations Global Compact	Global Compact (Intern. Org., 2000)	Companies	A voluntary initiative based on CEO commitments to implement 10 universal sustainability principles and advance “broader societal goals”, like SDGs.	Double Materiality
United Nations Environmental Program, Finance Initiative	UNEP FI (Intern. Org., 2005)	Investors	A partnership between UNEP and the global financial sector created in the wake of the 1992 Earth Summit with a mission to promote sustainable finance. Advocates Principles for Positive Impact.	Single Materiality with impact aspects
United Nations Principles for Responsible Investment	UN PRI (Network, 2005)	Investors	Founded by Global Compact and UNEP FI as a network of international investors working together to put six Principles into practice.	Double Materiality
Focusing Capital on the Long-term	FCLT Global (NGO, 2013)	Investors	Investor initiative which works to encourage a longer-term focus in business and investment decision-making by developing practical tools and approaches to support long-term behaviours across the investment value chain.	Single Materiality

Institution / Framework	*Acronym (Type, Foundation)*	*Actors directed at*	*Description*	*Materiality-lens*
Conceptual Frameworks				
Value Reporting Foundation, <Integrated Reporting> Framework	VRF / <IR> (NGO/Standard setter, 2010)	Companies	A global coalition of regulators, investors, companies, standard setters, the accounting profession and NGOs. Promotes multi-capital framework and value creation as the next step in the evolution of corporate reporting. Mission to establish integrated reporting as mainstream.	Single Materiality
European Commission, Non-financial Reporting Directive	NFRD EU Directive 2014/95/EU (EU Law, 2004)	Companies	Under the Directive, large European companies above 500 employees have to publish reports in relation to specific social and environmental information disclosure, as well as the policies they pursue to manage those.	Double Materiality
European Commission, Corporate Sustainability Reporting Directive	CSRD EU Directive (EU Law, est. 2022)	Companies	Under the Directive, all large European companies and all listed European companies have to publish reports on policies and metrics in relation to specific non-financial issues. The directive foresees a clarification of the concept of double materiality and to establish a mandate for non-financial assurance.	Double Materiality
Climate-Disclosure Standards Board	CDSB (NGO, 2007)	Companies	Works to provide climate change-related information into mainstream financial reporting. Offers companies a framework for reporting environmental information.	Single Materiality
Financial Stability Board's (FSB) Task-force for Climate-related Financial Disclosure	TCFD (Initiative, 2005)	Companies and Investors	Develops voluntary, consistent climate-related financial risk and opportunity disclosures for use by companies, banks, and investors in providing information to stakeholders. Works with scenario disclosures.	Single Materiality

Table 1. *Cont.*

Institution / Framework	*Acronym (Type, Foundation)*	*Actors directed at*	*Description*	*Materiality-lens*
World Business Council for Sustainable Development, Capitals Coalition	WBCSD Capitals Protocol	Companies and Investors	A global, CEO-led organization working to accelerate the transition to a sustainable world. Publish Natural Capital and Social & Human Capital Protocols which are frameworks for business to measure and value their non-financial impacts.	Double Materiality
International Standards Organization, Standard 14007 and 14008	ISO 14007 / 14008 (Standard)	Companies	Standard on determining and communicating the environmental costs and benefits associated with companies' environmental aspects, impacts and dependencies on natural resources and ecosystem services (14007); and Standard on monetary valuation of environmental impacts and related environmental aspects (14008).	Single Materiality
Data Standards				
Value Reporting Foundation, SASB Conceptual Framework	SASB (NGO /Standard setter, 2011)	Companies and Investors	Proposes industry-specific reporting standards for non-financial disclosure (topics and measures) with a focus on financial materiality. Standards are developed through multi-stakeholder consultation and updated periodically.	Single Materiality
Global Reporting Initiative, Sustainability Reporting Standards, G4	GRI (NGO /Standard setter, 1997)	Companies	Advocates for a sustainability reporting standard with a focus on materiality defined through externalities. They feature a modular and interrelated structure for reporting on a range of economic, environmental and social impacts.	Double Materiality

Institution / Framework	*Acronym (Type, Foundation)*	*Actors directed at*	*Description*	*Materiality-lens*
CDP (former Carbon Disclosure Project)	CDP (NGO, 2000)	Companies	Runs a global disclosure system for investors, companies, cities, states and regions to manage their environmental impacts. Its questionnaires help companies and investors understand climate related risks and opportunities.	Single Materiality
World Benchmarking Alliance	WBA (NGO, 2017)	Companies and Investors	An NGO which has set out to develop transformative benchmarks that will compare companies' performance on the SDGs. The benchmarks are to be backed by science, while leveraging existing international norms.	Double Materiality
International Financial Reporting Standards Board, International Sustainability Standards Board	IFRS ISSB (Standard setter, est. 2022)	Companies	An effort by the IFRS to establish standards for non-financial reporting by 2022. The approach will be based on the VRF template and pursue a single materiality and climate-first approach in standard-setting.	Single Materiality

aligned in most of the principles of practice. As an anchor for what constitutes a sustainable planet and society, many of these principles of practice reference the UN SDGs. This follows a larger trend, which suggests that the SDGs have become the primary global framework of reference for sustainability matters. A KPMG (2020) report finds that in 2020, 69 per cent of a global sample of 3,983 companies mentioned the goals in their corporate reporting, but the vast majority of companies referenced only their positive impacts on SDGs. These numbers indicate that companies are eager to demonstrate how they help solving social and environmental problems (positive SDG impacts), but they are considerably less forthcoming about how their activities might exacerbate these problems.

The conceptual frameworks for non-financial reporting and the data standards mentioned in Table 1 outline more specifically how to report non-financial information and which information to report. The most comprehensive non-financial reporting frameworks and measurement standards are offered by the Global Reporting Initiative (GRI) and the Value Reporting Foundation (VRF), which was created by a merger between the Sustainability Accounting Standards Board (SASB) and International Integrated Reporting Council (IIRC) in June 2021.[5]

Categories of how to structure measurement of non-financial information and guidance on how to report on key-concepts, such as materiality, will often be part of these frameworks. They are therefore important in guiding a company's view of its boundaries from a non-financial perspective. As such, different frameworks can be mapped to the different materiality lens they provide. Frameworks that are commonly viewed as describing a financial, single materiality view are the SASB Framework and the Taskforce for Climate-Related Financial Disclosure (TCFD). The GRI Framework is commonly viewed as focussing on a wider, double-materiality view. In addition, principles such as the SDGs, and regulatory advances, such as the European Commission's Green Taxonomy and the Non-financial Reporting Directive (NFRD), are advocating for a double-materiality perspective in their guidelines.

Regulation and standards for non-financial disclosure

With the proliferation of non-financial disclosure frameworks over the past twenty years, calls for standardising – and thus simplifying – the increasingly complex non-financial reporting landscape have grown louder. There is a wide consensus amongst investors, companies and other stakeholders that there is both a strong market-need

[5] Despite merging into one organisation, the frameworks are still separate tools (at the time of writing) and we thus refer to them as IIRC and SASB frameworks respectively in this paper.

and a demand for standards for non-financial disclosure. This was confirmed in all the interviews we led and the focus groups we observed. The assumption is that such disclosure standards ultimately have the purpose of providing a transparent and comparable data-environment for all stakeholders, while creating a level playing field for those companies under obligation to report on these standards. In our interviews the biggest asks for standards revolved around the creation of clear and explicit definitions, transparency around targets and aspirations, as well as the inclusion of legitimate benchmarks. The hope is that this would create consistency across organisations and time in reporting, allow the assessment of trends over time, link to a broader group of stakeholders in supply chain and beyond, and allow for external assurance of information.

Regulators and standard setters were initially slow to respond to these calls and companies and stakeholders have been confronted with a heterogenous set of largely voluntary disclosure frameworks. As late as 2018, senior representatives of IASB and Financial Accounting Standards Board (FASB) displayed firm resistance to the idea that financial standard setters should expand their mandate to the non-financial sphere.[6] However, since then a number of organisations, including standard setting bodies have significantly stepped up their efforts to harmonise non-financial disclosure frameworks.

The European Commission, in particular, has pushed for standardising non-financial disclosures in the European Union, launching an ambitious Sustainable Finance Action Plan in 2018 that comprises three interlocking regulatory initiatives. Firstly, the EU Taxonomy for sustainable activities is a classification system that determines the sustainability of economic activities against a set of environmental and social objectives. Providing detailed technical screening criteria for assessing the environmental and social sustainability of economic activities, the Taxonomy introduces a common language and benchmark for defining what is 'sustainable'. Secondly, the Sustainable Finance Disclosure Regulation (SFDR) defines the sustainability disclosure obligation of financial market participants and financial advisers towards end-investors. The SFDR is designed to harmonise the disclosure of sustainability-related information and partly builds on the Taxonomy. For instance, financial market participants offering sustainable investment products need to disclose how the underlying investment in an economic activity is impacting either an environmental or social

[6] In December 2018, an Oxford Union Debate saw eight high-level experts from the finance and accounting sector debate the following motion: 'This House believes that corporate sustainability reporting should be mandated, and standardised by FASB and IASB, for it to be most useful for investors'. The result of the debate was the following: two-thirds of the audience voted in favour of mandated non-financial disclosure by the international accounting standard setters. The representatives of FASB and IASB were largely on the 'nay' side of the discussion.

objective, as per the EU Taxonomy. Thirdly, the European Commission adopted a proposal for a Corporate Sustainability Reporting Directive (CSRD), which would amend the existing disclosure requirements under the Non-Financial Reporting Directive (NFRD). In comparison to the NFRD, the requirements in the CSRD proposal would apply to a considerably larger pool of companies, require disclosures to be audited, and align disclosures with a set of mandatory sustainability reporting standards. At the time of writing, these standards are being developed by the European Financial Reporting Advisory Group (EFRAG), but the CSRD proposals makes clear that any reporting requirements will need to be consistent with the Taxonomy and the SFDR.

Together, the three regulatory initiatives (Taxonomy, SFDR, CSRD) form the backbone of the sustainability reporting requirements that underpin the EU's sustainable finance strategy. While non-financial disclosure regulation is most advanced in Europe, other jurisdictions follow similar trajectories. For example, China, Malaysia and other jurisdictions (e.g. the UK) have developed or plan to develop taxonomies for discerning the sustainability of economic activities (OECD 2020; ICMA 2021). In North America, the U.S. Securities and Exchange Commission (SEC) announced in early 2021 that it would turn its attention towards the standardisation of non-financial disclosures and work 'toward a comprehensive ESG [Environmental, Social, Governance] disclosure framework' (Herren Lee 2021). At the time of writing, the SEC is expected to publish a proposal requiring climate-related disclosures – possibly modelled on the TCFD framework – in the near future (Latham & Watkins 2021).

In parallel to the EU's regulatory efforts, other leading providers of voluntary non-financial disclosure frameworks have also initiated work streams to bring their frameworks into closer alignment. In September 2020, a group of leading framework providers, including GRI, SASB and IIRC, issued a joint statement of intent to work together towards a comprehensive reporting system, which outlined an approach to arrive at a standardised set of non-financial disclosure requirements. Also in September 2020, the International Financial Reporting Standard Foundation (IFRS), published a consultation paper[7] to determine whether there was a need for sustainability standards and the role the Foundation could play in developing such standards. After receiving positive feedback on both accounts, IFRS Foundation established the International Sustainability Standards Board (ISSB) in 2021 to set global standards for sustainability measurement and reporting.[8] In April 2022, the ISSB delivered its first exposure drafts for global consultation. Responses to the consultation, which ended in July 2022, are currently being reviewed.

[7] https://www.ifrs.org/content/dam/ifrs/project/sustainability-reporting/consultation-paper-on-sustainability-reporting.pdf

[8] https://www.ifrs.org/news-and-events/news/2021/03/trustees-announce-strategic-direction-based-on-feedback-to-sustainability-reporting-consultation/

Together, these developments constitute an accelerating push for the standardisation of non-financial disclosure. And while agreeing on *what* companies should include in their non-financial disclosure is important, the standardisation of this disclosure is unlikely to be practically implemented without the corresponding technical clarity and sophistication in terms of *how* companies are supposed to measure, monitor, and report non-financial information. For example, it is one thing to agree on the need for greenhouse gas (GHG) emission disclosure, but it is another thing entirely to define exactly how GHG emissions are to be reliably and comparably measured across time and companies. And while GHG emissions are seemingly straightforward to measure and disclose, the most widely used approach for GHG emission reporting, the Greenhouse Gas Protocol,[9] is beset with problems of complex estimates and double-counting (Ramanna & Kaplan 2021). Similar challenges can be observed in the realm of climate risk disclosures. Although there is a growing consensus that companies need to disclose their exposure to climate risk and opportunities, it is less clear how companies can, for example, accurately measure the risk of local assets being impacted by the global increase in frequency and severity of extreme weather events. These technical challenges become even more pressing when considering corporate reporting on issues such as biodiversity or social impacts, where the complexity of the underlying systems magnify the difficulties of obtaining meaningful measurements and disclosures.

'Accounting' for purpose

In the previous section we noted that viewing materiality in relation to purpose gives legitimacy to both single and double materiality perspectives and therefore the simultaneous measurement of a firm's impact and its financial viability in relation to non-financial goals. To retain a societal license to operate, however, organisations cannot merely focus on the achievement of positive impacts but must also recognise and account for the negative externalities.

While some externalities are slowly priced in through market-mechanisms (i.e., carbon prices), others are still largely ignored by the market and should therefore be recognised at the entity level. This poses numerous challenges for both financial and management accounting. The challenges straddle issues faced both by preparers of financial statements for external financial reporting purposes and those faced by internal decision makers and management accountants. In this section we review some of these challenges, for financial reporting and management accounting side. This leads

[9] https://ghgprotocol.org/

into a discussion of some new methodologies of multi-capital accounting for externalities that seek to address these problems and what their limitations are.

Purpose in financial reporting

Under current accounting practices not all economic events are recognised in financial statements. Some of the limitations exist due to uncertainty around identifiability, measurability and control. Take the recording of investments as an example. While many purpose-relevant metrics are connected to specific corporate investments in things like renewable energy sources, waste-water management systems, employee training programs, under current accounting standards, not all of these can formally be recorded as investments. This has to do with the treatment of expenditures. In financial accounting, an investment classifies an allocation of economic resources into either a physical assets, land, financial assets, intangibles, or other companies, with the hope and intention that these would appreciate (create a financial return on investment) with time. This means that only very specific types of expenditures can be classified as investments and capitalised, that is, recorded as an asset on a company's balance sheet and depreciated (or amortised in the case on intangibles) over its estimated useful life. Expenditures that don't meet these criteria are treated as expenses, thereby reducing net profit in that financial period.

Accounting for expenditures on fixed assets or certain types of stand alone intangibles is straightforward and these can be recorded as an asset and with some approximation a useful economic life determined. Similarly, operating expenses are normally straightforward to identify and expense as incurred. However, not all expenditures fall neatly into one or the other category, and principles of prudence and conservatism require that if there is uncertainty about future economic benefits and ability to control an asset, the expenditure should be expensed through the income statement. This creates several challenges for accounting for purpose: management is disincentivised to invest in social and environmental management, as it has direct consequences for the bottom line, and long-term management of the value of social and environmental assets is neglected as they are not carried on the balance sheet.

There is extensive literature about the treatment of non-financial and intangible assets of a company. For example, from a purpose-driven management perspective, investment in training employees is viewed as an investment in social and human capital for the company and the employees. This investment would be expected to yield positive operational results and should therefore be capitalised. In financial reporting practice, however, training costs are generally expensed as incurred (as operating expense, through the income statement). Although there has been wide-ranging discussion about whether these could and should be capitalised, the recurrent accounting issue is that while internally generated intangibles are likely to yield future returns, these future economic benefits cannot be reliably measured and the assets cannot be controlled (e.g., employees can leave). Therefore, most costs incurred in creating these intangibles are treated as expenses. According to the IASB and FASB conceptual frameworks for something to meet the criteria of an asset the reporting entity needs to be able to control it directly or indirectly, it should generate future economic benefits, and fulfil criteria such as identifiability and separability (IAS 38, IASB). The identification of an intangible might be subject to interpretation and judgement and depend on legal criteria in different jurisdictions. Often due to their subjective nature they are not fully accounted for, thereby, potentially leaving gaps in the balance sheet.

A recent discussion paper[10] of the UK Financial Reporting Council (FRC) highlights the challenges of reporting intangibles and proposes 'realistic' solutions from a current accounting perspective. The FRC paper however acknowledges the constraints in reporting for intangible assets, especially where the definition of an asset is constrained by the conceptual framework. At a practical level, because of the uniqueness and subjectivity of intangibles (what should be considered an intangible asset, and what shouldn't), there is considerable variation in the practice of measuring and recognising intangible assets. New types of businesses, technological developments and innovation mean that it is almost impossible to have an exhaustive list of different intangibles, and prescriptive methodology on how to measure and account for each of these quickly becomes dated. The challenges facing accounting for intangibles are not dissimilar to those pertaining to the accounting for externalities and impact, which face similar concerns of measurement and objectivity. Due to these challenges, the discussion around the measurement of externalities and impacts is in nascent stages, and under current practices there is no straightforward way by which human, social and natural capital derived intangibles can be recorded.

Purpose in management accounting

Effective management accounting is fundamental to good decision making on several dimensions such as resource allocation, product and service mix, and pricing. At the heart of this is a detailed and accurate understanding of a firm's costs, and this understanding is based on cost characteristics such as the traceability, nature and behaviour, and purpose of costs. Analysis of these costs is not straight forward, and changing business and economics conditions have thrown up various challenges. Broadly speak-

[10] Financial Reporting Council, 6. February 2019, Discussion Paper – Business Reporting of Intangibles: Realistic Proposals https://www.frc.org.uk/consultation-list/2019/discussion-paper-business-reporting-of-intangibles, last accessed May 2019.

ing, costs fall into the categories of direct and indirect, fixed and variable, as well as product or period costs. However, costs are often much more complex than this and do not easily fit into these groups.

Insight into the functionality and purpose of the vast variety of costs is crucial in internal decision making. In addition to problems with identifying and measuring these internal costs in their various categories, further difficulties arise when interfacing these costs with information that is included in the company's financial statements. Certain disconnects exist between financial and management accounting, and practitioners use several marginal and relevant costing principles for internal decision making that are not identical to costs presented for external reporting purposes. The inherent conflict between management needing to make decisions that are beneficial in the medium to long-term and reporting positive results to shareholders in the short run, creates distorted incentives and possible misallocation of resources (Johnson & Kaplan 1991; Johnson 1994).

Considerable research literature and practice has been devoted to understanding and updating our methodologies and toolsets to analyse and measure these costs as we have moved from a post-war manufacturing to internet-based and intangibles-intensive world. Adding to this, the complexity and conflicts inherent in incorporating natural, social, and human costs raise considerable challenges. The costs of these externalities cannot be readily derived from market prices because the underlying factors are not necessarily traded in deep and liquid markets. Still, the knowledge and incorporation of such non-financial factors is increasingly important for management accounting, particularly to manage long-term risks and to avoid profiting from social and environmental harm. Selected methodologies on how to incorporate these measures are presented below.

At present there is no single accepted path for accounting for costs – especially those in the human, social, and environmental space. Models and methodologies for cost-based non-financial accounting are therefore largely advanced and advocated for by the academic community, not by the profession itself. Some companies acknowledge the importance of expanding our understanding of costs and resource consumption beyond the narrow view traditionally taken and make use of proprietary methodologies to do so. The practical motivation for companies is often couched in noble motivations – ending poverty, preserving the earth's resources, building society – rather than tied to the notion of purpose. The challenge remains in capturing all these factors in 'accounting acceptable terminology'. The following marks an account of suggested methodologies which value and incorporate non-financial concerns into accounting practices in various ways.

Frameworks and methodologies for multi-capital accounting and valuation

The last ten years have seen the development of a variety of multi-capital reporting and accounting frameworks that could enable full cost accounting, economic valuation, and capital maintenance. Most of these frameworks seek to facilitate the incorporation of negative and positive impacts of business operations on the material non-financial capitals (or assets) of a business. Papers by Stroehle & Rama Murthy (2019) and Barby *et al.* (2021) list and categorise a variety of these frameworks which seek to monetise non-financial information around performance. Organisations currently active in the space are, amongst others, the Value Balancing Alliance (VBA), the Economics of Mutuality (EoM) foundation, the Harvard Impact-Weighted Accounts Initiative (IWAI), and the Banking for Impact (BFI) project. Broadly speaking, these frameworks put forward two methodologies through which corporate externalities can be expressed in financial terms: (1) capital maintenance (building on logics of full cost-accounting), and (2) impact valuation. In the following discussion we evaluate how and whether these methodologies are useful in measuring performance in relation to notions of purpose, and what conceptual and practical concerns remain.

Capital maintenance and full-cost accounting

Barker & Mayer (2017: 12) lay out a cost concept for sustainability accounting, which is defined as 'a system that measures, reports and reconciles business activity from both a financial and a sustainability perspective'. The methodology outlined in this paper underpins the British Academy's principle on performance and purpose. A truly sustainable profit therefore accounts for negative externalities around material human, social and natural capital to provide a view of 'profit net of harm'.[11] In this approach, 'the important point is that monetisation is concerned specifically with the cost of making good any physical depletion of the natural resource; at heart, therefore, the notion being employed is that of physical capital maintenance […]' (Barker & Mayer 2017: 15). The theory of change focusses then on the incorporation of capital maintenance (CM) processes and the provision of their cost on corporate income statements, through which companies set strong incentives for their business executives to act and manage the firm according to its purpose. Through this, companies can assess *the cost of externalities to the business*, and create a monetary value for the single materiality lens.

[11] Refer to description of 'Materiality' earlier in this paper.

According to the CM principle, all renewable non-financial capital assets that are owned by a company are replaced upon consumption. Consumption of the asset is expensed, while the sales value of the asset is recognised as income (Barker & Mayer 2017). The cost-based adjustment of the income statement includes two entries: the cash inflow from customers and the capital outflow which is spent to replace the asset. If the company were to choose not to replace the non-financial capital and instead accept depletion, then a hypothetical replenishment cost would appear on the adjusted income statement until the maintenance is performed. If non-financial capital is not easily renewable (i.e., the use of coal has no logical replacement), cost-based sustainability accounting can refer to the necessity of business transformation. In this case, the focus would lie on investments in non-financial capital and internal or external capacity building in order to find ways in which businesses can change their reliance on non-replaceable natural assets.

CM for social and environmental assets builds in its logic on the so-called Full Cost Accounting (FCA) approach which aims to capture the external impacts of organisational actions on society and the natural environment. As such, FCA is part of wider efforts to account for externalities, which seek to complement conventional financial accounting systems by capturing the 'social, environmental and broader economic impacts arising from the activities of an entity that are borne by others and do not feedback directly into short-term financial consequences for the entity' (Unerman *et al.* 2018: 498). While measures to internalise externalities have been extensively discussed by economists at the national level, FCA is a concept from the social and environmental accounting literature focused on 'incorporat(ing) all potential/actual costs and benefits including environmental (and perhaps social) externalities' (Bebbington *et al.* 2001b: 8).[12] This also links to earlier notions of Sustainable Cost Calculation, which 'provides calculations of what additional costs must be borne by the organisation if the organisational activity were not to leave the planet worse off, i.e. what it would cost at the end of the accounting period to return the planet and biosphere to the point it was at the beginning of the accounting period' (Gray 1992: 419).

Impact valuation

Rather than using the notion of cost to assign monetary values to externalities, the methodology of impact valuation (IVA) uses impact multipliers (such as shadow

[12] While the term FCA was coined by Bebbington *et al.* (2001) in the early 2000s, attempts to incorporate social and environmental impacts into corporate accounting practices can be traced back to the 1970s (Antheaume 2007).

prices) to estimate the magnitude of impact a firm has on its ecosystem. It therefore represents the flipside of capital maintenance and FCA: rather than representing the cost to business, IVA estimates *the cost of externalities to society*. The assumption being that if externalities are not valued by the market, then companies need to value them in order to communicate how their actions impact on stakeholders. This form of monetisation therefore serves the double materiality view.

Methodologies that attempt to undertake an economic valuation of natural and social impact do so by either observing or approximating market prices through hedonistic techniques, or they use survey-based pricing techniques that assess the stated preference, the revealed preference and changing consumer behavioural patterns in relation to certain externalities (VBA 2021). Particularly in the latter approaches, stakeholders themselves play a central role in determining the shadow price and value of an externality through, for example, assessments of willingness to pay, willingness to accept or induced purchasing behaviours. Antheaume (2004) further discusses the application of three such valuation approaches – avoidance cost method, cost of damages method, and collective consent to pay method – in an experiment that examines the environmental impact valuation of an industrial process concerned with feeding natural gas into domestic gas distribution networks. While the three methods discussed differ in their specific design, they all rely on valuing environmental impacts as economic consequences for third parties through the financial implications for societal actors.

The idea of valuing non-financial impacts and dependencies in monetary terms relates in many ways to the responsibility of knowledge. According to a prominent promoter of impact valuation, Sir Ronald Cohen, the information that IVA offers can help to shift investment decision towards "the adoption of a new paradigm of risk – return – impact" (Cohen 2018: 15). Having a balanced view of IVA alongside risk return is argued to aid in decision making and can facilitate comparison between diverse categories of impact and dependence. It is also believed to help contextualise decisions, where different economic and political environments under assessment may warrant different weights for certain impacts. Apart from management accounting IVA is also proposed as a valuable insight for the investor sphere. The Harvard Impact-Weighted Accounts Initiative (IWAI), which uses the impact valuation methodologies to adjust financial accounts to get an 'impact-weighted' view of corporate performance, argues that valuation of this kind 'translates all types of social and environmental impacts into comparable units that business managers and investors intuitively understand' (Serafeim *et al.* 2019).

Challenges in the monetisation of externalities

We show above how different monetisation methodologies can be useful to help organisations take into account both the cost of their externalities to society (IVA and IWAI) and their cost to the business itself (CM and FCA). We also highlight how the latter represents a single materiality view, whereas the former represents a wider, double-materiality view. This suggests that both methodologies are needed for comprehensive measurement of purpose. CM and FCA can be used to create an adjusted view of the profitability of a purpose solution, describing it net of the costs absorbed that were needed to maintain natural and social capital and therefore avoiding a notion of profiting from harm. IVA and IWAI are useful to assess whether targeted solutions actually create the desired impacts, and whether there may be any unintended consequences or externalities of the venture that would need to be taken into consideration by the management team. While the necessity and usefulness of monetisation for the use of purpose may seem relatively straight-forward, there are a number of conceptual and practical challenges associated with these methodologies.

Conceptual challenges

On a conceptual level the literature on FCA argues that there are limitations to the commensurability of social and environmental impacts through monetisation (Frame & O'Connor 2011). Unerman *et al.* (2018) point out that the intersubjective consensus required for achieving commensurability might be impossible to establish for some externalities, given the high level of context-specificity of issues such as water use or biodiversity. Furthermore, they argue that in the absence of 'a process of widespread intersubjective consensus-building, the resulting objectified externalities accounts risk being misleading as well as non-comparable' (Unerman *et al.* 2018: 510).

Secondly, the commensurability of social and environmental impacts is enmeshed with moral and ethical considerations (Antheaume 2007). While the monetisation of impacts has clear advantages in terms of complexity reduction, i.e. it translates different impacts into a common language, it also poses serious ethical questions. For instance, can negative impacts in one area be compensated by positive impacts in another area? Is it possible, or desirable, to offset negative environmental impacts with positive social impacts or vice versa? Can, or should, a stable climate be traded-off against positive corporate tax contributions? Depending on the philosophical, political, and ideological commitments of an observer, the answers to these questions will differ profoundly. Likewise, while '[i]t can be argued that placing a value on such things as life or biodiversity is not morally acceptable as these attributes may have an infinite value' (Antheaume 2007: 214), there are frameworks – such as, for example, the VBA approach – which argue that 'the value of a statistical life has been used by policymakers around the world when deciding whether regulations to reduce the likelihood of fatalities are worth the costs of implementing them' (VBA 2021: 23), and that such hedonic pricing is important to make informed policy and business decisions.

Finally, FCA and IVA have a political dimension which manifests itself both in terms of processes and design choices. On a processual level, this gives rise to the question of which stakeholders are involved in the construction of full cost accounts, that is, who has a say and whose voices are heard (Bebbington *et al.* 2007). Closely related to this processual aspect is the issue of choosing the most relevant design features of FCA approaches, including which impacts are considered and how these impacts are assessed (Frame & O'Connor 2011).

Practical challenges

The practical challenges of FCA and IVA include technical difficulties, social dynamics involved in implementing new accounting systems, and organisational and institutional context factors. Firstly, technical difficulties stem largely from data availability issues, both in terms of physical impact data as well as financial data to monetise these impacts (Bebbington *et al.* 2001; Herbohn 2005; Frame & Cavanagh 2009). Academic case studies of FCA implementation attempts are relatively scarce and empirical settings are often public or public-private entities such as a New Zealand-based research institute (Bebbington & Gray 2001), an Australian government department (Herbohn 2005), or infrastructure projects in New Zealand (Frame & Cavanagh 2009). Despite the relatively modest size of the entities under investigation in these studies, a lack of data still constituted a serious impediment, often contributing to the failure of implementing FCA within these organisations. Technical challenges associated with data availability are even greater in the case of globally operating companies with complex and dispersed value chains.

Furthermore, social dynamics can manifest themselves in the form of internal and external stakeholders' resistance against the implementation of FCA. For example, in a case study of the implementation of FCA in an Australian Government Department in charge of managing publicly owned forests, resistance against FCA emerged from outside the organisation in the form of adversarial conservationist stakeholders and from sceptical managers within the organisation, who both expressed philosophical reservations against monetising aesthetic aspects of forests (Herbohn 2005). In addition, organisational and institutional contexts can interact with both technical and social factors in obstructing the implementation of monetisation. External developments such as political pressures and resource constraints can limit the room for experimentation within organisations and distract managers' attention away from implementing new accounting systems (Herbohn 2005). Contextual factors such as resource constraints seem to be particularly relevant in corporate settings, where take-over threats or economic downturns can result in a strong focus on financial cost control, thereby reducing the scope for dedicating resources to projects that might be seen to pay off only in the mid- to long-term.

Finally, frameworks developed among private companies (such as the Mutual profit and loss statement of the EoM foundation) are often developed for business operations on project level, and are very granular and difficult to aggregate and report, which is challenging for comparability. Valuation techniques try to address these problems, yet standards would be necessary to transcend from entity-level methodological decisions. This is where the logic of organisations such as the VBA and projects such as the Harvard IWAI comes to action. Only time will tell how successful they can really be in creating methodological standards without either wide market acceptance or institutional intervention.

Performance, materiality and purpose in practice

In this section we discuss how notions of sustainability-related materiality and concerns about social and environmental issues and externalities are applied in three core areas: investment practice, corporate governance and corporate decision-making. We assess current practice to understand whether the notion of corporate purpose is actually considered, and – if not – whether and how it would help to design more holistic performance measurement. We use the notion of the investment chain to review how information flows from companies to different capital market participants, and we review the incentive structures that are created through the practices that consider this information.

Since capital allocation from investors is key to enable corporate purpose at the organisational level, it is important to understand how the concept of performance is constructed by investors when they look at matters of social and environmental concern, and how this influences management and decision-making at the corporate level. We first examine notions of non-financial performance and materiality in investment practice through the relationships between asset managers and asset owners. We then shift the focus from investment practice to corporate governance, and in this we explore the role of boards in the adoption of corporate purpose and discuss the implications of this for the company's fiduciary duty. Finally, we examine how senior management can implement purpose-oriented policy and decision-making throughout a company by focusing on the role of non-financial metrics in intra-organisational processes and incentive structures.

Rethinking performance along the investment chain

There are many actors that make up the investment chain, including a wide variety of investment intermediaries and advisors that create a complicated network of transactions in capital markets (Arjalies *et al.* 2017). Notwithstanding, much of the investment incentives are still set between asset owners, asset managers and companies. Asset owners are usually large capital owning entities (such as pension funds or sovereign wealth funds) who invest on behalf of a beneficiary population (such as pensioners or a specific government and its people). Asset managers usually manage funds of asset owners and high net-worth individuals. They do so through either active or passive investment strategies that make use of a mix of asset classes. Asset owners usually give asset managers an investment mandate to allocate their capital in a certain way: for example, with high risk and maximum returns, or as long-term, stable yield, or under consideration of specific sustainability concerns.

Financial markets participants have been a major driver of non-financial disclosure as both asset owners and asset managers increasingly seek to incorporate non-financial factors into their investment practices. Some investors seek to incorporate non-financial factors to reflect their moral concerns, and others use so-called sustainable or ESG investing practices to manage long-term risk within their portfolios. While the actual environmental and social impact of this investment practice is contested (Busch *et al.* 2016; Koelbel *et al.* 2020), the importance of financial markets as enablers of capital moving towards more sustainable and transformative businesses and innovation strategies cannot be underestimated. Controlling the allocation of significant amounts of financial capital (Hawley & Williams 2007), asset owners have been proclaimed as key drivers behind the efforts to integrate non-financial considerations into investment processes (Clark & Hebb 2005; Lachance & Stroehle 2021). This argument often cites the 'universal ownership' thesis (e.g. Hawley & Williams 2007), where large institutional investors have such highly diversified and global portfolios that they are inevitably exposed to large systemic risks, such as climate change, and therefore have an inherent fiduciary duty to track and address these in an effort to minimise their exposure and help create positive transformation.

Despite the growing interest in sustainable investing practice, many challenges remain. Firstly, there are major data problems. To incorporate sustainability-objectives into their capital allocation decisions, asset owners and asset managers need high-quality, consistent, and comparable non-financial metrics. Current ESG datasets are subject to much criticism, as their scores vary widely (Chatterji *et al.* 2016; Berg *et al.* 2019) and their methodologies are opaque and change over time (Eccles & Stroehle 2018; Berg *et al.* 2020). While it is argued that the standardisation of non-financial metrics would be helpful for strengthening the reliability and validity of ESG performance assessments (Busch *et al.* 2016), there is doubt whether it will help investors identify purposeful and long-term sustainable business models. And while most large asset owners and asset managers have made some kind of commitment towards sustainability-related goals, actual capital allocation – especially in asset classes beyond public equity – often paint a much less earnest picture that lead to greenwashing concerns. For example, in July 2021, Bloomberg reported that the fund-classification rules of the SFDR led to a drop of US $2 trillion in ESG-related funds in Europe – suggesting that many of those were previously labelled green without sufficient rigour in the underlying ESG assessment.[13]

Secondly, incentive structures in the financial markets are often not aligned with sustainable finance objectives. For this to change, clear mandates from asset owners to asset managers, including expectations towards the integration of ESG considerations and engagement practice are needed. Ideally, the contracted parties would set up some due diligence processes and reporting alongside these requirements as proof of their integration strategies. However, since asset managers usually deal with more than one asset owner at a time, due diligence processes are often flawed, and asset managers are given considerable freedom as to how to implement their mandate. There are also concerns about relatively short time-frames of mandates which clash with the long-term asset management logic of sustainable capital allocation. More and better disclosure from asset owners and asset managers regarding their sustainable investing activities could also lead to more stakeholder pressure and direct capital to those investors with the more ambitious sustainability targets.

Thirdly, for sustainable investments to not only avoid bad companies, but to actually induce change, capital allocation needs to be embedded in a broader notion of stewardship. Stewardship activities flank investment activities with stakeholder collaboration, advocacy, and particularly, engagement and voting (Eccles *et al.* 2021). In addition to encouraging corporate disclosure of non-financial metrics, asset managers therefore, increasingly engage with companies on questions regarding their long-term strategy and value creation. Academic evidence (Gond *et al.* 2018) suggests that effective and long-term ESG engagement can create important value for shareholders, particularly through three dynamics: (a) communicative dynamics – engagement enables the exchange of information between corporations and investors, creating

[13] Bloomberg, 2021, European ESG Assets Shrank by $2 Trillion After Greenwash Rules. https://www.bloomberg.com/news/articles/2021-07-18/european-esg-assets-shrank-by-2-trillion-after-greenwash-rules

‘communicative value’; (b) learning dynamics – engagement helps to produce and diffuse new ESG knowledge amongst companies and investors, creating ‘learning value’; and (c) political dynamics – engagement facilitates diverse internal and external relationships for companies and investors, creating ‘political value’. However, since the disclosure of material issues from companies is often minimal, engagement efforts from different investors at the same company can diverge strongly. This may limit the effectiveness of singular engagements on specific issues with companies, particularly if conversations are one-off and comparable to a box-ticking exercise. As a result, joined investor initiatives, such as Climate Action 100+, have become more popular to drive common engagement strategies on specific issues.

While corporate purpose is now also increasingly championed by the investment world,[14] there is little evidence to suggest that purpose is used as an investment criteria, and materiality frameworks used by investors are often exclusively focussed on single materiality (i.e., which non-financial issues impact firm value and performance). Still, developments in capital markets suggest that sustainable investing is becoming more holistic and we argue that a purpose-lens could be helpful in supporting these trends. Firstly, impact investing strategies have grown significantly over the last years,[15] specifically focusing on companies that provide solutions to problems of people and planet. Secondly, double materiality disclosure is increasingly mandated by regulatory frameworks, particularly within the EU,[16] and investors can take this information into account more readily. And thirdly, due to the growing importance of stewardship,[17] corporate purpose can offer a powerful lens to investors to holistically assess a company’s business model and potential for long-term value creation.

[14] Most prominently supported by BlackRock’s CEO Larry Fink, who stated in his 2019 letter to CEOs that ‘Purpose is not a mere tagline or marketing campaign; it is a company’s fundamental reason for being – what it does every day to create value for its stakeholders.’ And that it was BlackRock’s fiduciary duty to ‘help clients to invest for the long-term’. https://www.blackrock.com/americas-offshore/en/2019-larry-fink-ceo-letter.

[15] The Global Impact Investor (GIIN) Survey 2020, for example, suggest that impact investing has grown by 17% in 2020 alone. https://thegiin.org/assets/GIIN%20Annual%20Impact%20Investor%20Survey%20 2020.pdf

[16] See, for example, the European Commission’s proposal for the Corporate Sustainability Reporting Directive and its view on double materiality: https://ec.europa.eu/commission/presscorner/detail/en/ QANDA_21_1806

[17] See, for example, the UK Stewardship Code from 2020 and its principle one in reference to ‘Purpose, strategy and culture’. https://www.frc.org.uk/getattachment/5aae591d-d9d3-4cf4-814a-d14e156a1d87/ Stewardship-Code_Dec-19-Final-Corrected.pdf

Purpose and performance in corporate governance

As environmental and social concerns become more important for shareholders and stakeholders alike, there is increasing need and demand for corporate boards to outline how their companies are positioning themselves on these issues. If boards chose to engage with these issues, the importance of performance in relation to purpose is particularly relevant for them on three levels: (1) for the fulfilment of their fiduciary duty, (2) for the formulation and implementation of strategy and purpose, (3) for engagement with investors and for communication to stakeholders.

The board's fiduciary duty is a key piece in the consideration of the environmental and social performance and impact of a firm. While since the 1970s, fiduciary duty was overwhelmingly viewed as the board's responsibility to act in the interest of shareholders, this viewpoint has been overturned in recent years (Eccles & Youmans 2016). In the 2016 UK Corporate Governance Code, as well as in Section 172 of the UK Company's Act, the legal responsibility of boards is outlined as applicable to all stakeholders of their firms, not just to shareholders. While UK law is particularly progressive in this regard, changes are also seen elsewhere. A 2019 legal memo of the US law firm Wachtell, Lipton, Rosen & Katz, for example, underlines a broader notion of boards' responsibilities by discussing a significant decision of the Delaware Supreme Court interpreting the *Caremark doctrine*: The Court said to 'satisfy their duty of loyalty, … directors must make a good faith effort to implement an oversight system and then monitor it themselves ... , the existence of management-level compliance programs is [therefore] not enough for the directors to avoid Caremark exposure'.[18] This legal decision highlights the expanded notion of boards' responsibilities, even in the relatively more conservative legal system of the United States. Lipton (2019: 2), and outlines that directors must: 'recognize the heightened focus of investors on "purpose" and "culture" and an expanded notion of stakeholder interests … and work with management to develop metrics to enable the corporation to demonstrate their value.'

The changing expectations of company boards and directors in the context of responsible stewardship and governance were further clarified by the Enacting Purpose Initiative (EPI),[19] a research project which engaged board members on the role of purpose. The initiative's reports (2020; 2021) underline that boards increasingly recognise the mounting expectations they face to formulate a credible corporate purpose and strategy. They also recognise that it must go beyond a mere empty pledge, such as seen by the Business Roundtable in August 2019, where 181 CEOs pledged to a more

[18] http://www.wlrk.com/webdocs/wlrknew/WLRKMemos/WLRK/WLRK.26467.19.pdf, last access Aug 2019
[19] http://www.enactingpurpose.org/

holistic, stakeholder-oriented version of the 21st century corporation yet never adopted any meaningful changes thereafter. The EPI suggested a SCORE framework that highlights how boards can enact purpose through five core principles: Simplify purpose, Connect to strategy, Own purpose at the board level, Reward purpose and Exemplify it through practice (Eccles *et al.* 2020). The framework therefore highlights the importance of connecting purpose to both materiality and performance.

Current practice suggests, however, that boards seldomly link purpose with measurement. Because of this, many directors feel ill-prepared to address or discuss sustainability issues. Without clear objectives and targets, it is difficult to link purpose to strategy and to communicate progress in relation to purpose to investors and other stakeholders. It is therefore the link of purpose with materiality and non-financial data within an organisation which can help the board deal more confidently with the most material non-financial concerns. Some have suggested that the creation of a board-signed Statement of Purpose would be a good start for companies to control the narrative around who they think their significant stakeholders are (rather than just saying 'all stakeholders' matter) and what material issues the firm recognises and intends to make a priority in accordance with its purpose.[20] The Statement can also be used to communicate timelines (what the company understands as 'long-term') and be informed and evaluated by the use of non-financial metrics, allowing both alignment within the company and more targeted conversations with stakeholders outside the organisation.

The importance of purpose measurement for management decisions

As previously discussed, both financial and non-financial metrics play a critically important role in informing and guiding corporate decision making to achieve corporate purpose. While financial measures are routinely reviewed, it is important for businesses to also have a strategic approach to managing both non-financial targets in their own entity, as well as multi-capital accounting frameworks and impact valuation. Stroehle & Rama Murthy (2019: 10) therefore argue that many sustainability accounting frameworks

> … have concentrated on the measurement of non-financial capitals. The management of these non-financial capitals is [however] a separate stream of research. Managing businesses to tackle societal and environmental concerns is explored as shared value or system value. Practice tools such as Future-Fit can help companies to pursue social and environmental goals and track extra-financial information for internal and external audiences.

[20] Hermes Investment, 2019, https://www.hermes-investment.com/ukw/wp-content/uploads/2019/08/statement-of-purpose-guidance-document-aug-2019.pdf, last accessed October 2019.

The emphasis on embedding non-financial measurement into management frameworks directs attention towards ways in which non-financial metrics are being used within companies. A helpful concept in this context is the notion of management controls, which 'include all the devices and systems managers use to ensure that the behaviours and decisions of their employees are consistent with the organisation's objectives and strategies' (Malmi & Brown 2008: 290), or in other words, the company's purpose. Put differently, the sheer availability of non-financial metrics within organisations might inform behaviour but it does not automatically shape practices and, ultimately, decision-making: 'While information systems may have an influence on behaviour, they are not specifically designed to hold organisation members accountable for their behaviour, nor do they relate behaviour to targets' (Malmi & Brown 2008: 295). Hence, non-financial measures need to be embedded in control structures that incentivise managers to consider these metrics in their decisions-making.

If measures are chosen according to their materiality and linked to corporate purpose this can, for instance, be used to integrate relevant non-financial objectives into (individual) performance targets, which, if achieved, unlock additional compensation, benefits and promotion. Purpose then becomes an essential component of incentivising and evaluating managers and staff and ultimately analysing firm performance. Furthermore, material purpose targets can be integrated into key management processes, such as strategy development, capital expenditures and risk management. The recommendations of the TCFD, for instance, ask companies to disclose how climate-related risks and opportunities are considered in governance, strategy, and risk management processes.

Through these practices we observe that increased understanding and scholarship on embedding purpose through multi-capital frameworks into performance frameworks may see positive effects in decision making across the investment chain. These frameworks could result in better long-term decision making on corporate investments such a capital expenditures. The challenges arise in creating environments where a large proportion of firms commit to these expanded management frameworks, and asset owners and managers are incentivised to take these into consideration when making investment allocation decision. This entails an environment of rigour and transparency in evaluating purpose driven performance from corporate decisions through to asset owner level.

Conclusion

The performance principles of corporate purpose suggest that measurement needs to reflect whether companies take into account the growing significance of workers, societies and natural assets both inside and outside a company's legal boundaries, and that performance should be evaluated in relation to attainment of corporate purposes and profits measured after providing for costs of rectifying failures to fulfil them. This paper examines the practicability, limitations and feasibility of these principles by arguing that they are linked to three separate measurement considerations. In a first instance, performance measurement needs to focus on the attainment of a problem solved, as set out through a company's purpose. These measures will be non-financial in their own entities as well as impact-related to understand whether a given business solution has (un)intended consequences. Second, purpose measurement must be linked to a notion of profitability (although adjusted) and therefore to the idea of single materiality and how the firm's value and performance is influenced by its surroundings. Third, purposeful companies need to take account of their externalities by absorbing the cost of maintenance in relation to natural and social assets, and by assessing and managing their impact in relation to their values to society.

We find that while the demand for non-financial reporting and disclosure is growing rapidly and progress to provide this information has been made both in regard to regulation and standardisation, considerable gaps and challenges persist for actors at various levels to link these measures and activities to purpose. Corporate purpose is still often seen and treated as a marketing tool: a high-level commitment to broad sustainability-related goals, yet without any tractable commitments made in its relation, nor any linked incentive structures. For purpose to be real it would have to be considered in the way investors allocate their capital sustainably, in the way boards set 'the tone at the top', formulate strategy goals and fulfil their fiduciary duties, and in the way managers are incentivised and evaluated.

Purpose without measurement runs the risk of being merely a mirage, or quickly side-lined as soon as a more important (financial) concern arises. With the framework we outline, we show that it is not impossible to establish measurement of purpose, in particular when performance in relation to purpose is linked to existing frameworks of measurement and notions of single and double materiality. Getting this implementation and measurement right is absolutely key, as we need to have good measurement of long-term value-creation and public accountability for corporate externalities if we want to successfully address the system-level challenges we are currently facing.

Acknowledgements

This research was commissioned and funded by the 'Future of the Corporation' programme of the British Academy. All related online content of the programme can be found under: www.thebritishacademy.ac.uk/programmes/future-of-the-corporation/research

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Appendix 1. Examples of corporate practice

Name	*Novo Nordisk*	*Olam*	*Mars*	*Value Balancing Alliance*
Organisation type	Publicly listed company	Publicly listed company	Private company	Association (e.V.)
Industry sector	Healthcare	Food	Consumer goods	Non-profit organisation
Purpose of the organisation	Driving change to defeat	Re-imagining global agriculture and food systems	Our Consumer is Our Boss	Integrating business into society and environment by developing a standardised impact measurement and valuation model that enables decision-makers to create and protect long-term value
Headquarter	Denmark	Singapore	USA	Germany
Countries in which the organisation is present	80	>60	80	Member companies operate globally
Organisation annual revenues	111,831 million Danish kroner	S$30.5 billion	> $35 billion	Annual budget of approximately €800 000
Total numbers of employees	43,202	74,500	125,000	15 plus extensive stake holder network
Extra-financial measurement innovation	Application of the Future-Fit Business Benchmark, a measurement approach that translates system-level requirements of sustainability into clear organisation-level objectives, thereby offering a practical tool for assessing how companies contribute to solving societal key challenges as defined in the UN SDGs.	Integrated Impact Statement (IIS) that comprises both a Profit and Loss (P&L) and a Balance Sheet approach to measuring Olam's short- and long-term impacts and dependencies on various capitals, including human, social, and natural capital.	Mutual Profit & Loss (P&L) tool as an additional internal management account for measuring and managing performance across human, social, natural, and shared financial capital.	Development of a standardised Impact Measurement and Valuation (IMV) model to monitor, manage, and disclose the economic, environmental, human, and social value companies provide to society.

Appendix 2. List of interviews and focus groups

Expert interviews

Organisation: Deloitte. *Name:* Veronica Poole, Global Head of IFRS. *Interview date:* August 2019

Organisation: Deloitte. *Name:* Neil Stevenson, Director Deloitte UK. *Interview date:* August 2019

Organisation: Hermes Investment Management. *Name:* Dr Michael Viehs, Associate Director. *Interview date:* August 2019

Organisation: Impact Management Project. *Name:* Clara Barby, CEO. *Interview date:* September 2019

Organisation: International Integrated Reporting Council. *Name:* Charles Tilly, CEO. *Interview date:* September 2019

Organisation: The Prince's Accounting for Sustainability Project. *Name:* Jessica Fries, Professor of Accounting, Executive Chair. *Interview date:* August 2019

Organisation: University of Oxford. *Name:* Professor Robert Eccles, Visiting Professor of Management Practice and Founding Chairman of SASB. *Interview date:* August 2019

Organisation: University of Oxford. *Name:* Professor Richard Barker, Professor of Accounting. *Interview date:* August 2019

Organisation: Value Balancing Alliance. *Name:* Christian Heller, CEO. *Interview date:* September 2019

Observed focus groups

British Academy, London, Future of the Corporation Workshop on Measurement & Performance. *Date:* May 2019

British Academy, London, Future of the Corporation Workshop on Measurement & Performance. *Date:* June 2019

British Academy, London, Future of the Corporation Workshop on Principles. *Date:* September 2019

To cite the article: Stroehle, J.C., Soonawalla, K. & Metzner, M. (2022), 'Through the looking glass: tying performance and materiality to corporate purpose', *Journal of the British Academy*, 10(s5): 87–123.
https://doi.org/10.5871/jba/010s5.087

Journal of the British Academy (ISSN 2052–7217) is published by
The British Academy, 10–11 Carlton House Terrace, London, SW1Y 5AH
www.thebritishacademy.ac.uk

Journal of the British Academy, **10(s5)**, 125–161
https://doi.org/10.5871/jba/0010s5.125
Posted 26 August 2022

The purposeful corporation and the role of the finance industry

David Pitt-Watson and Hari Mann

Abstract: The finance industry—banks, insurers, fund managers and the rest—play a pivotal role in our economy. In particular they have a profound influence on the behaviour of our corporations and the individuals that work for them. To provide its services, the finance industry has considerable powers in corporate governance. So, if we are to reconceptualise the purpose of the corporation, this article argues that we also need to do the same for the role of the finance industry. The article begins with a review of the limited literature around 'the purpose of the finance industry'. It then poses the question about what that purpose should be, whether the industry's current practices are adequately fulfilling that purpose, and how this affects corporate behaviour. The article argues that if the finance industry itself were more purposeful, that would help to promote purposeful companies. Finally, the article makes a series of recommendations on how stakeholders can create a model of change within the industry to support purposeful outcomes.

Keywords: Finance, purpose, trust, purpose of finance.

Note on the authors: see pp. 155–6.

Introduction

This article was commissioned as part of the Future of the Corporation work stream at the British Academy.[1] The programme examines the need to reconceptualise the purpose of the corporation around three connected principles: well defined purposes, a commitment to trustworthiness, and an enabling culture.[2] By doing this, corporations can continue their contribution to the development and prosperity of society. The central premise of this article is that to create more purposeful companies, a finance industry is needed which supports their creation.

The influence of the finance industry is huge. Companies require finance to survive. They need it to fund the development of new and existing activities and to provide the system in which financial transactions can be undertaken. Here finance is the 'enabler' to the economic functions of the corporation. Finance also plays a role in 'shaping' the behaviour of the corporation. The powers given to shareholders can have a profound influence on how companies behave. Shareholders approve the board, auditors and incentives given to directors, and hence influence the overall strategic direction of the firm, its activities and business models, and hence its purpose.

Just as we reconceptualise the purpose of the corporation, we need to do the same for finance. This article begins with the same critique as the Future of the Corporation. That is that we need to pose questions about the purpose of the finance industry because we cannot trust that market forces alone will guide the industry to its desired destination. We will argue that if the finance industry itself were more purposeful, that would in itself help to promote purposeful companies. In doing so, it would support the recommendations of the Principles for Responsible Business as set out by the British Academy,[3] in particular principle 7, that:

> Corporate financing should be of a form and duration that allows companies to fund more engaged and long-term investment in their purposes.

The central aim of this article is to examine the evidence for the argument we have set out above. To do so, we will structure the article as follows. First, we will define the functions of the finance industry. Second, we will present our review of the literature into the purpose of finance to provide a context to the arguments being made. Third, we will explore who the industry is there to serve and in particular its role in providing funds to companies and its use of the powers accorded to it to provide those funds. Fourth, the article will set out what a purposeful finance industry might look like and

[1] British Academy (2018a).
[2] British Academy (2018b).
[3] British Academy (2019).

how far the current industry is from the one we seek. To do this, we will examine how the institutions of finance provide funds and exercise stewardship. We will look at whether the shift towards Fintech will provide solutions. Fifth, we will recommend reforms which will make the finance industry more purposeful. Finally, we will discuss how this underpins the principles laid out by the Future of the Corporation, and suggest the next steps for this work.

1. What is the purpose of the finance industry?

'What is the purpose of the finance industry?' For other industries we are able to address this question in a straightforward manner. For instance, the motor industry builds machines which transport us from A to B swiftly, efficiently, conveniently, safely and in comfort, without hurting others. We measure its performance by its ability to build better, more efficient cars year-by-year. We might also say that in the future, it will continue to have this purpose, fulfilling it better through technological advances such as electric and driverless cars. Whether an engine uses petrol or a battery, the core purpose of the industry remains the same, with electric cars fulfilling the function in a way which minimises emissions. Other examples abound, from the healthcare industry which serves the purpose of curing the sick, to the hospitality industry which serves the accommodation of guests, and so on. Reflection might lead us to conclude that we know the purpose of most industries. Doubtless there can be some debate about precise goals, and how they are best measured. But the overall purpose of industries is usually clear, providing a metric against which success can be measured.

However, in our experience, and in subsequent research which we will discuss, the evidence suggests that if you pose this question of the finance industry, you will likely be given a range of responses. Indeed for many, there may even be a question of what constitutes the 'finance industry'. We would define it as all those institutions whose principle function is the management of money. That includes banks, insurers, investment managers and pension funds. It also includes investment banks, hedge funds, private equity managers, and stock markets. It encompasses much of the audit, accounting and actuarial professions. It includes brokers and financial advisors. Taken together, they account for around 7 per cent of the UK GDP.[4]

But what is the purpose of all this activity? Those cynical of the industry will say it's for the purpose of paying large salaries, their argument fuelled by media stories focusing on remuneration in the sector. The majority of people may tell you they just

[4] House of Commons Briefing Paper No. 6193, Contribution of the Financial Services Industry to the UK Economy (2021). https://researchbriefings.files.parliament.uk/documents/SN06193/SN06193.pdf

hadn't asked the question about what finance was for. And since they hadn't asked the question, they hadn't answered it either.

Since 2017, we have asked this question to a diverse range of audiences (further details are given in Appendix 1), from practitioners in financial institutions, to politicians, to academics, to perhaps the most important stakeholders, the customers the finance industry serves.[5] It is clear that there is consensus among them that the purpose of finance is a topic worthy of debate. There is also a consensus that it would be useful to define the purpose of finance. And it is also clear to us that it is a question that few have yet answered.

So why do we struggle when we are asked about the purpose of finance? Is it that we haven't given the subject enough thought? Is the answer too complex, or is it that we may uncover a gap between the purpose of finance and current reality? History shows that, similar to the corporation, many of the early institutions of finance were clear about the purpose of their activity and what they were providing to their customers. Yet, the evidence we have collated finds that today's institutions and those who work in them are unclear of what the purpose is. For us to develop our argument that creating purposeful corporations requires a purposeful finance industry, we set out our thinking around what the purpose of finance might look like.

Let us firstly lay out our current thinking as to the functions of the finance industry. This draws on the history of the finance industry – the first services provided by banks, for example – and by observing the services finance is beginning to provide in the world's emerging economies. We see four essential functions (Figure 1).

The first is the safekeeping of assets. We sometimes take for granted that we have institutions like banks which we can give our money to, and who will keep it safe. That is an essential service, and it is one that was unavailable to most people throughout history and remains so today for many people in many countries. Within the UK, quite recent estimates suggested that as many as two million adults still do not have a bank account, relying exclusively on cash for their daily transactions.[6] And it is not only banks we rely on to keep our money safe. We also expect institutions such as pension and investment funds to hold our financial assets and act as custodians, albeit on different terms from a bank.

The second function follows from the first: it is to provide an effective payment system. Again, this is a service that we take for granted in the developed world. Yet without it, modern commerce could not survive. We can see its value by looking at situations where the service has been lacking. In Kenya today, migrant workers can transfer their funds back to their families using their mobile phones, through which

[5] Pitt-Watson & Mann (2017).
[6] Financial Inclusion Commission (2015).

Figure 1. The purpose of finance.

they also receive their salaries. In the past, this process involved guards taking cash to pay them their salaries, and then a complex process for getting the monies back to their respective families.[7]

The third function of the finance industry is its ability to allow us to share risk: to allow us to buy life, car or house insurance, so that if disaster strikes, we have something in compensation. To allow us to have a pension that will last us until the day we die. Business also benefits from risk sharing, for example insuring factories or ships at sea. As a result, we can avoid many of the worst consequences of life's catastrophes.

The fourth, and perhaps the most important function provided by the finance industry is that of intermediation: matching users and suppliers of money. Put simply, intermediation is about how we 'take money from point A where it is, to point B where it is needed'.[8] This process is of enormous value. At its most simple, it can be combining savings deposits and helping individuals buy homes or businesses buy assets. It allows economies to grow. It allows for social mobility. Before modern banks, assets were simply passed from generation to generation. What social mobility there was

[7] Hartley (2012).
[8] Rothschild (1977).

amounted to a process of everyone raising themselves by their bootstraps. So intermediation is of profound importance not just to the global economy, but also to society.

Our research presented these functions of finance to various audiences. Whilst we do not argue that we have created the definitive taxonomy on the purpose of finance, it provides a basis for discussion, and builds the argument for the connectedness between a purposeful finance system and purposeful corporations. The four functions can be combined in different ways to provide different financial products. In the simple case of someone who opens a bank account, they not only have their money kept safe, they are also enabled to transact with customers and suppliers. In turn their savings will be intermediated to provide funds for others.

Companies can raise either permanent (usually equity), or repayable (usually loan) capital. In raising that finance, it will often give significant power to those who have provided the capital, which will in turn influence behaviour.

2. Literature review on the purpose of finance

As part of our research, we looked at what academic work had been done on the 'Purpose of Finance'. Given the large number of academic institutions teaching and researching finance, we hoped the literature might help us reflect on the functions of finance and how these can best be delivered to create a purposeful outcome. We therefore commissioned two studies of the literature, one in 2017 and more recently, a more in-depth review of academic journals in 2019.

In Appendix 2, we discuss the approach taken. By no means is this an 'absolute' or 'exhaustive' review of the literature. It does, however, help to build our hypothesis that there remains a scant number of sources, be they from academics or practitioners that discuss this question in any structured rigorous fashion.

Throughout the literature, there is a general agreement that the purpose of finance is to serve the outside world. For example, in his book, *Finance and the Good Society*, Shiller (2012) states, 'Finance is not about making money per se … it exists to support other goals-those of society'. It provides 'stewardship to protect and preserve the assets needed for the achievement of and maintenance' of individual and societal goals. Purpose is thus very broadly conceived. Others take a similar approach. Dembinski (2009) argues that 'a healthy financial sector serves both the common good of society, as well as the wellbeing of individuals who participate in it'. Beinisch & Biehl (2012) say that a narrow view of the purpose of finance is 'to create and preserve wealth' but that it also has wider functions, 'such as the development of the wider economy, social harmony and stability'. These broad definitions, while emphasising the broad influence of the industry, are of little help in defining specific, measurable goals.

The finance literature itself is more specific in defining functions. Although language differs somewhat between authors, all have an overlap with the six functions defined by Nobel Prize winning economist, Robert Merton (1995) and later again by Merton and Bodie. Those are to:

1. provide a payments system
2. pool funds for investment in large indivisible projects
3. transfer resources through time and across geographies and industries
4. manage uncertainty and risk
5. provide information in a decentralised system
6. manage asymmetric information.

Many introductory economics textbooks discuss the functions of finance as the matching of borrowers and savers, or in other words moving funds from people who have a surplus to people who have a shortage, which might fall under Merton's third function.[9] Others suggest additional purposes, such as providing liquidity, or developing new processes.[10] Some are more specific in describing the approaches the industry must take in fulfilment of its goals, Naik (2008), for example, notes that risk can be managed only by diversification, that is by sharing it.

Kay (2015) offers a list of four functions, consistent with, and perhaps more practical than those suggested by Merton: managing a payments system; matching lenders and borrowers; helping us to manage personal finances, and the risks associated with everyday life and economic activity.

Within the finance literature, there is a stream of literature around financing of the firm and how this affects its nature.[11] They nonetheless still struggle to make more explicit links to the purpose of a corporation and the nature of the finance industry that funds it. Having reviewed ten of the most prominent journals in finance (listed in Appendix 2), we found literature that discussed the nature of the firm and parts of the finance system, instruments of the finance system, and associated theories around it. But there was nothing that drew together the corporation and finance system, and analysed the dependency and interconnectedness of the two systems.

We would also make two further comments on the literature. First, there is a danger that it conflates 'enabling functions' in finance, such as successful innovation, or the management of asymmetric information, with the ultimate services it provides for the outside world, such as providing a payments system.

[9] Mishkin (2004a); Ireland (2008); Bradfield (2007).
[10] Epstein & Montecino (2016).
[11] Rajan (2012).

Second, and related to that observation, there is a danger that some of the externalities in undertaking the functions of finance, particularly the positive ones, are themselves viewed as purposes. For example, certain forms of intermediation allow price discovery, just as trading vegetables in a market allows price discovery; knowing market prices may have positive side effects, but price discovery is not a primary purpose of finance. The same might be said of 'the separation of ownership and management', which intermediation makes possible, and the concomitant requirement to 'monitor the management' if such separation is to prove safe. We would again not dispute the value of separation, or the necessity of monitoring. But we would view them as enablers of an effective system of intermediation rather than as ends in themselves.

But perhaps our most significant observation is that we have found no studies which, having defined the functions of finance, have gone on to measure systematically how well the industry has performed its role. Some, for example Kay, offer examples where the finance industry appears to be less than purposeful. But Merton and Brodie, and indeed the textbooks of finance have a tendency to assume that, having defined the purpose of finance and having noted that financial markets are competitive, it can be assumed that this 'will cause the changes in institutional structure to evolve towards greater efficiency in the performance of the financial system'.[12] In other words, the finance literature reflects the critique central to the Future of the Corporation Project. It does not 'pose questions about where we are going because, like a blind man guided by the invisible hand of a good Samaritan, [through markets and competition], we are led to our desired destination'.[13]

At this point we should offer a caveat. While this conclusion holds good for most of the mainstream literature and curriculum in finance, there are those who understand that whatever the advantages of markets, alone they will not lead to the 'desired destination'. Often, they offer a critique of the operations of the finance industry. Some are economists; we have mentioned John Kay's excellent analysis. Others study the sociology of finance, noting that the activities of the industry often do not result in the optimal outcomes. But while this work is important, little of it is incorporated into mainstream finance.[14] None of it is framed explicitly around the question of the purpose of finance, and how it can be measured.

We have found only one set of studies which have sought to measure efficiency in a way that is directly related to how the finance industry performs its functions. In particular that of Thomas Philippon (2015), to whose work we will refer later on in

[12] Merton (1995).

[13] British Academy (2019).

[14] For example, of the thirty-six scholars contributing to the *Oxford Handbook of the Sociology of Finance*, only four were members of finance or accounting faculties.

this article. However, with that possible exception, we have discovered few studies of the efficiency of the finance industry overall which have started by defining either the functions or the purposes against which efficiency might be measured.

For the reasons given above, and because of the nature of Merton and others' categorisations, the task of measuring the performance of the finance industry is extremely difficult. That in turn makes it problematic to assess whether or not finance is fulfilling its functions or working efficiently. This is a huge gap in our knowledge, and one which might be considered a major stumbling block to anyone—for example a regulator—whose aim was to make the industry perform better.

That is why we have suggested our own set of purposes for finance. All of these are functions which directly benefit the outside world. All of them are ones which are, at least to some extent, measurable. We would note that different financial products incorporate a variety of functions to fulfil their purpose. For example, a pension system will be required to keep our money safe, to intermediate, and to allow risk sharing, particularly as regards longevity risk. Other functions will have important enabling functions; thus, while the ultimate purpose of a stock exchange is to assist effective intermediation, it does this by allowing effective price discovery and appropriate levels of liquidity.

We would note that, absent any definition or measurement of function or purpose, it is difficult to prescribe what changes to the financial system will be beneficial. For Merton (1995), and for previous writers, this problem has just been ignored, or assumed away by positing that competition will always lead towards a more efficient system. However, as we shall see, the evidence suggests that this assumption is unsafe.[15]

3. Evidence of the effectiveness of the finance industry in delivering purpose

It is difficult to conceive of a modern economy which lacks an effective financial system. Indeed, its services are so beneficial to society that many early entrepreneurs who started financial institutions were known as philanthropists. They sought to address the problems people faced when they couldn't get access to financial services. Examples are littered through history, from the first 'people's bank', the Trustee Savings Bank set up by a Scottish minister to serve his flock, to the work of Grameen Bank's Mohammed Yunus, which provides capital to the poorest of Bangladesh through micro-finance. What Yunus was doing was not, in theory, different from a

[15] (1) For example Mishkin (2004a), or Bradfield (2007). (2) For example Vandekerckhove *et al.* (2012). (3) For example Mishkin (2004b).

loan shark. In theory the same, in practice totally different. One has a clear and positive purpose, the other undertaken with little regard to the welfare of the consumer. Of course the finance industry is not alone in offering products which seem to be of little benefit. Indeed market economies often allow poor products to be introduced. But if markets work well, poor products do not survive for long because those which fail to meet consumer needs fall by the wayside.

It is this process of 'creative destruction', as described by Schumpeter (1942), which ultimately leads to improvements in quality and lowering of price. And those improvements can be measured. We can note over time the greater speed, safety and comfort of a car, and its lower cost and emissions. We can chart the growing efficacy of drug treatments, and are rightly scandalised when mis-prescription occurs. In the case of finance, similar improvements should be apparent.

Yet as we shall see, the evidence, both anecdotal and empirical, suggests that the finance industry not demonstrating such improvements. The Chair of the UK's chief financial regulator suggested that much of what was taking place was 'not socially useful'. The President of the American Finance Association has made similar comments.[16] The head of the US Federal reserve that financial innovation was largely rent seeking.[17] Their comments are supported by empirical data from Thomas Philippon (2015) who has discovered little or no increase in the efficiency of intermediation in over a century, thus implying that the finance industry that funded the construction of railways over 120 years ago had a similar level of productivity to the one which today funds the internet. We will return to these issues later. But before doing so we need to address the question of who the finance industry is there to serve; how a purposeful system would interact with the companies to whom it provides finance; the gap this suggests with current practice; and finally what measures might help to fill any such gap.

3.1. Who is the finance industry there to serve? What are their likely needs and how might this affect company financing?

It is generally acknowledged that the purpose of the financial system is to serve the outside world. In particular its central role, and the one which gives it most influence over company behaviour is its role in providing them with funds, which will in turn support purposeful output.

The chart in Figure 2 is a simplified illustration of this system of intermediation. On the left are those who have excess cash which they are saving, or who are using the

[16] Zingales (2015).
[17] Volker (2019).

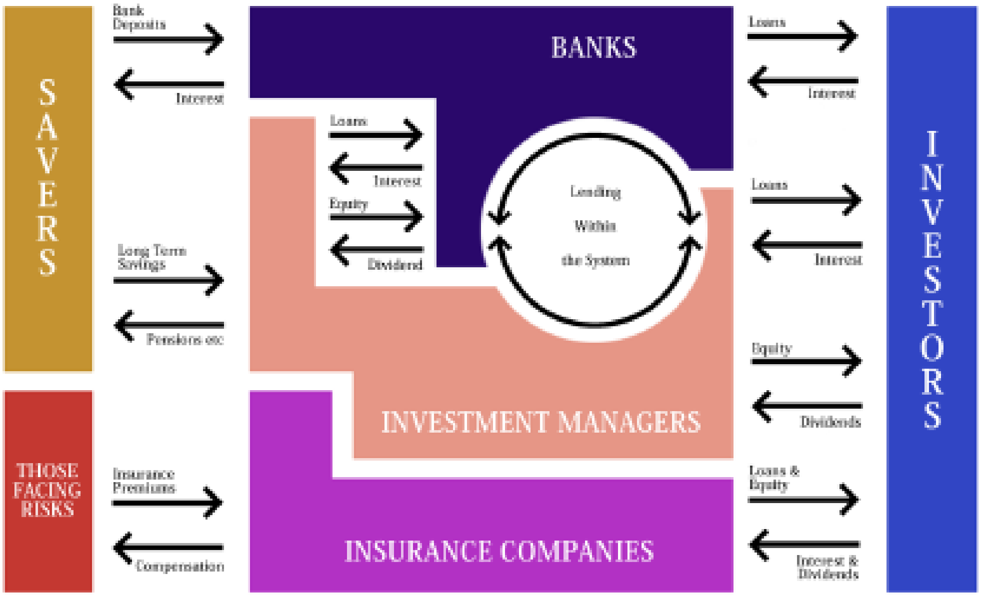

Figure 2. The financial system.

financial system to hedge against some unforeseen risk; on the right the users of those savings, typically companies, or households which are borrowing. The finance industry thus has two sets of customers: the providers of funds and the users of funds.

We would note that if the financial system is to be stable, then it is a necessary condition that the promises it makes to those providing funds must be matched by the promises it accepts from those who use those funds. Where this is not the case, specific protections need to be put in place. So for example, a bank can accept short term deposits, and lend long term only if it knows that the central bank will come to the rescue if everyone decides to withdraw their deposits.

Therefore, when providing funds to companies, the financial system needs to be careful that the terms on which finance is provided match the obligations due to those who have provided the funds. With that, it is worth reviewing the nature of the savings made by savers, since this will, and indeed should affect the type of finance offered to companies. (In this example we have concentrated on some key characteristics of UK savings. We recognise that the financial system is globalised, and that a full analysis would review all sources of funds. This is beyond the scope of this article.)

In the UK household private financial and pension wealth amounts to around £7.0 trillion. Of that £5.4 trillion is represented by pensions, £1.6 trillion by other assets.[18] As regards the pension wealth, on our estimates, around £3.25 trillion of that

[18] Office for National Statistics (2018).

is funded—i.e. supported by financial assets.[19] So some two thirds of financial assets are provided from the pension system. The scale is prodigious. For example, the combined wealth of the Top 1000 families in the *Sunday Times* Rich List, is around £0.77 trillion, less than a quarter of funded pension wealth.

We would note that pension promises are long term; indeed the 'average life' of an open pension plan might be around 25 years. We would also note that most families in Britain have some pension provision. Finally, we would note that most pensions are invested in many hundreds of different companies, in order to reduce the risk of any one of them failing.

Thus, as far as the UK is concerned, a financial system that was serving its purpose for those providing funds, would be likely to be long term in its perspective (reflecting the long term nature of pension liabilities), it would be cognisant of the need to serve the many millions who needed a pension, and thus of the importance of upholding a purposeful corporate system, where profit was not being made through zero-sum game activities, or by externalising costs.

3.2. What is the role of the finance industry in providing funds to companies and what powers are accorded to the industry to fulfil this role?

The financial system must also cater for the need of the users of funds: households, companies and governments. Our particular interest is in the way they fund and influence companies.

There are two principal instruments through which funds are provided to companies: Debt and Equity. Debt is provided either by borrowing from a bank, or larger companies can raise money by issuing a bond. In both cases, there are strict contractual terms as regards interest repayment and security. Bonds are often tradeable; hence, the owner of the bond can realise its value, (albeit at an unknown price) should the need arise.

Equity is permanent capital. Unlike a bond, the cash flow it will generate is not contracted. Rather the directors of a company have a fiduciary duty to serve the interests of all the equity holders in their company (not just the biggest shareholders), as well as giving consideration to other stakeholders.[20] Equity holders are, in turn, given significant powers. They elect directors. They approve the auditor. They discharge the board through the approval of annual accounts and have various other powers.

[19] Some is the promise made by the government to fund public servants pensions, and some represents the underfunding of other pension plans.

[20] A fuller definition of directors' duties is given in the Companies Act, in particular Sec 172 CA (2006).

Equity holders receive a financial reward through the payment of dividends. In the case of public companies, they are able to sell their shares at the market price.

Equity holders thus have huge influence over the way the company is run. These powers are only lost if the company is unable to pay its debts, in which case powers fall to the creditors, typically led by the bank or the bondholder. Either way, the financial system is very influential. The *Principles for Purposeful Business*[21] suggest that the power of the financial system might ultimately be reduced to help support purposeful companies. In this article we ask a related question which is whether a financial system which focused on purpose, might itself promote the emergence of purposeful companies.

4. What might a purposeful finance system look like? In particular how will it support investee companies?

We have already noted that, given the nature of saving into the financial system, the funding of companies might be likely to be long term in its perspective (reflecting the long term nature of pension liabilities). It would be cognisant of the need to serve the many millions who needed a pension, and thus of the importance of upholding a purposeful corporate system, where profit was not being made through externalisation or zero-sum game activities.

Finance will, of course, continue searching for returns in order to meet pensions and other liabilities, but if it is serving the interests of the provider of funds, it will not promote these at the expense of the society in which its savers live. So how might we envisage such a system would work? Below we cite three examples of its likely behaviour.

Stewardship principles of an institutional investor

One institution which has been quite explicit about the characteristics it wishes to see from the companies it invests in is Federated Hermes (formerly Hermes Fund Managers). These are expressed in the Hermes Principles,[22] which lay out explicitly what investment institutions should expect of public companies, based on the needs of the many thousands of people whose pension funds it managed.

The Hermes Principles are adamant about the rights of shareholders and the need to generate value over the long term. Their starting point is enlighted shareholder

[21] British Academy (2019).

[22] Hermes Principles (2002)

value on behalf of many savers. However, they are clear that profit should not be made by externalising costs, and that stakeholders should be treated fairly.[23] They also insist on the need for companies to be clear about their strategy, and the need to focus on those activities where they have a competitive advantage.

The Hermes Principles might suggest that a purposeful financial system would be supportive of purposeful companies provided that purpose was not pursued at long term private and social expense to shareholders. In this case, shareholders are defined as the many millions of people saving for a pension.

Universal ownership

Similar themes emerge from those who have noted the degree of diversification of pension and other investment portfolios, and the behaviour which this should engender. This is often described as Universal Ownership (UO) Theory. A helpful discussion of the literature on Universal Ownership can be found in an article by Ellen Quigley,[24] which discusses its significance for fund managers considering how they might respond to environmental issues. Universal Ownership notes that many institutional investors own 'a more or less representative slice of the economy and cannot reasonably sell out of individual companies. In particular, they would wish to discourage 'companies whose activities add costs to … other companies in its portfolio'.

Universal Ownership has some theoretical downsides, for example it might encourage monopolistic practices.[25] However, it is also likely to find investors championing solutions to systemic risks, which damage portfolios rather than just individual companies.

Indeed, one might see this in action in the efforts of investors to find a solution to global warming. Very large groups of investors have promoted more radical climate action,[26] and have lobbied companies to cease investing in fossil fuels.[27] Thus, a

[23] The Hermes principles were written by one of the authors of this report. As regards ethics, they state that 'ethical behaviour by companies is likely to involve some notion of fairness and reciprocity; that managers seek to understand the position of those whom their action affects, and that they deal fairly with them'.

[24] Quigley (2019).

[25] See for example the arguments made about airline pricing (Stanford Graduate School of Business 2019). The authors of this article regard any causal conclusion from this study to be questionable. It has found only one example of the phenomenon (by accident there should be many incidents given the level of diversification of funds). Nor have they suggested any mechanism by which fund managers would encourage companies to raise individual product prices.

[26] For example Ceres, or the Institutional Investor Group on Climate Change.

[27] For example Climate Action 100+.

combination of the very large number of savers, and the broad diversification of investment means that a purposeful financial system will promote many of the characteristics of the purposeful company, provided that purpose is not achieved at a private or social cost. We should therefore turn our attention to the cost of pursuing the purposeful corporation, and whether there is a cost to equity holders of doing so.

Is pursuing purpose costly to shareholders?

And indeed the evidence suggests there is little evidence that profit comes at the expense of purpose. Quite the reverse. While we should be cautious about the data, a survey of the literature on purpose and performance has been undertaken for the Big Innovation Centre (2016). Far from discovering that there was a trade-off between purpose and profit, it concludes that while the evidence is not definitive, 'the payoffs from purpose are … reflected in share price performance, improved accounting and operational performance, more valuable innovation and lower cost of capital'. In his recent book, Professor Alex Edmans of London Business School (2020) concludes that, 'based on the highest quality evidence … it's not an either-or choice – companies can create both profit and social value. The most successful companies don't target profit directly, but are driven by purpose – the desire to serve a social need and contribute to human betterment.'

So, provided that it took a long-term view of company profitability, rather than encouraging a short-term jump in share prices, a purposeful financial system should promote purposeful companies. Indeed that is already the language that it is speaking. For example, Larry Fink, is CEO of Blackrock, the largest fund manager in the world, which holds around 5 per cent of global shares in thousands of companies ultimately representing many millions of savers. In his annual letter to the leaders of those companies, he urges them to view purpose as 'the company's fundamental reason for being. Purpose is not the sole pursuit of profits, but the animating force for achieving them'.[28] Critics may say that such statements have yet to be adequately demonstrated in practice. Nevertheless, the desired direction is clear.

In theory then the characteristics of our financial markets would suggest that at least in theory, they should encourage the promotion of purposeful companies. They should be long term since the average life of an investment is long term. They should be sensitive to social issues, in particular to accountable governance. They won't want to profit at customers' expense.

[28] Fink (2019).

Financially they will still seek profits. Companies cannot decide to be charities. However they will seek profit through purpose rather than at its expense, and note, with Larry Fink that, ‘in fact profits and purpose are inextricably linked’.

Some may suggest this view is overly optimistic, even Panglossian. However, it does suggest that the problem which needs to be addressed is not occurring because the characteristics of financial markets are necessarily inimical to purposeful companies. Rather the big gap, and (pragmatically) the easiest to address is not the gap between purposeful finance and purposeful companies. It is the gap between the finance industry we have today, and the purposeful one it ought to be. Unless that gap is filled, it will prove difficult to promote purposeful companies.

4.1. How far is the finance industry today from the purposeful one we seek?

As mentioned above, there are few, if any, studies that define and measure how well the finance industry is performing its basic functions, let alone how well these are translated into purposeful activity. If we were to rely on popular perception, the results would be grim. In a Bank of England study, citizens were asked to choose one word to describe the likely future of the finance industry, and its development. The most popular word chosen was ‘corrupt’ (Figure 3).

As mentioned previously there is one study which aims to measure the efficiency of the financial services industry. It was undertaken by Thomas Philippon of NYU (2015) and has been repeated for European countries by Guillaume Bazot (2018). It begins with the assumption the purpose of the finance industry is to serve the outside world, and that the principle service it provides is to intermediate: accepting money

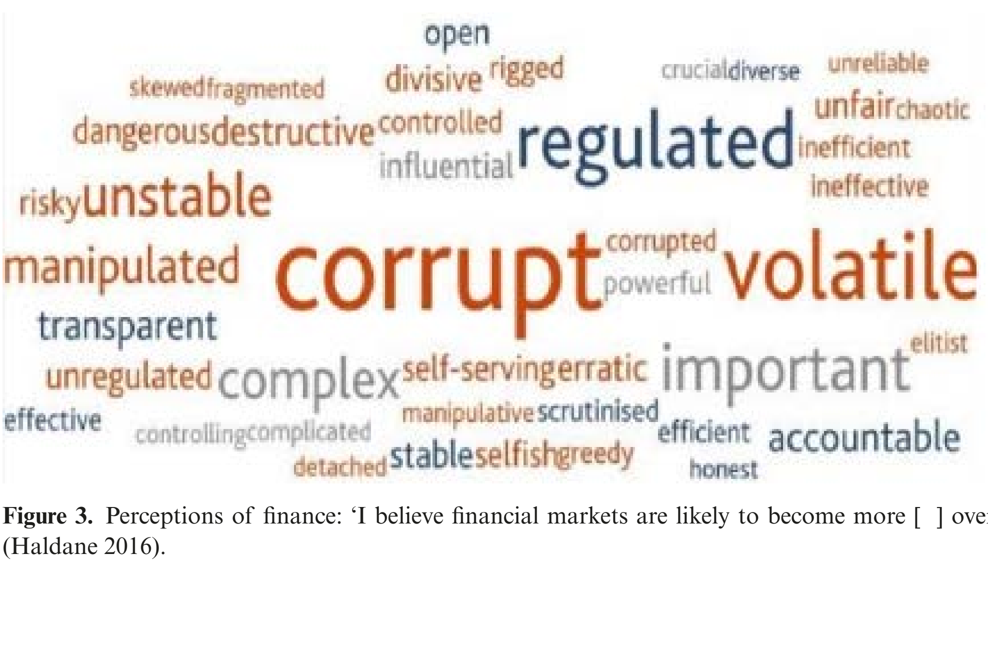

Figure 3. Perceptions of finance: ‘I believe financial markets are likely to become more [ ] over time’ (Haldane 2016).

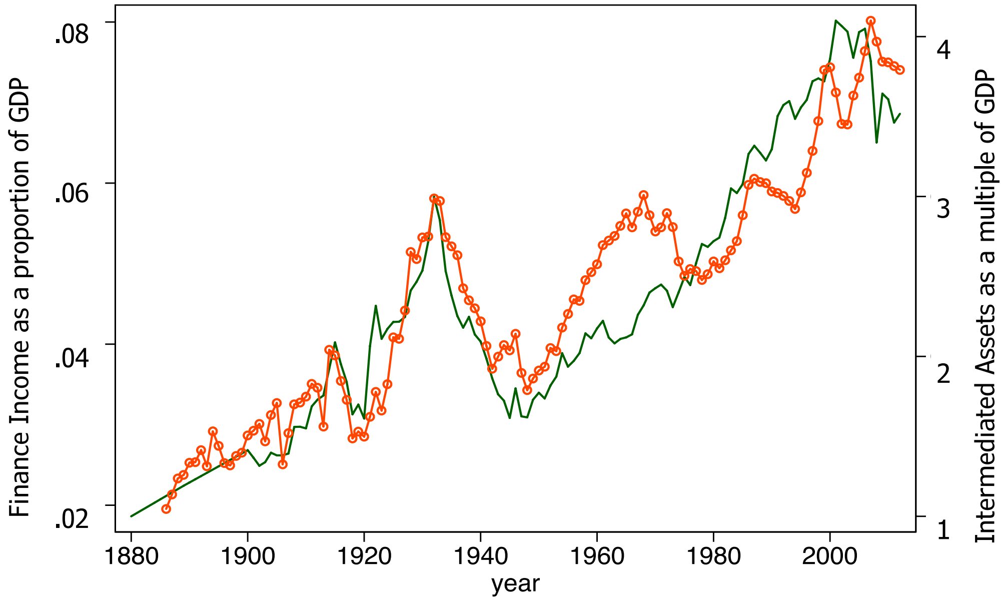

Figure 4. The scale of the US finance industry and funds intermediated as a percentage of GDP.

from those who save, and placing it with those who invest. Philippon tracks the amount of 'net' intermediated funds in the USA over 130 years today (i.e. eliminating any borrowing or lending which takes place within the financial system itself). As Figure 4 shows, the scale of intermediation has increased considerably, from around one times the GDP in 1880 to four times.

Figure 4 also shows the cost of running the finance system has also grown from 2 per cent of GDP in 1880 to 8 per cent today. Since the growth in the money intermediated, and the growth in the aggregate cost of the finance system are approximately the same, this suggests that there has been little improvement in the productivity of the finance industry over 130 years, illustrated in Figure 5. Philippon's numbers adjust for the mix of borrowing and lending, but this makes little difference to the overall conclusion. At the aggregate level, and despite technological improvements, little productivity improvement is discernible.

With this evidence in mind, it is interesting to reflect on Paul Volcker's observation on the industry (2009). Volcker was formerly Chair of the Federal Reserve Bank of the USA.

> I found myself sitting next to one of the inventors of financial engineering … I knew who he was and that he had won a Nobel Prize. I asked what all the financial engineering does for the economy and what it does for productivity. Much to my surprise he [said] it does nothing. I asked him what it did do and he said that it moves around the rents in the financial system and besides that it was a lot of intellectual fun.

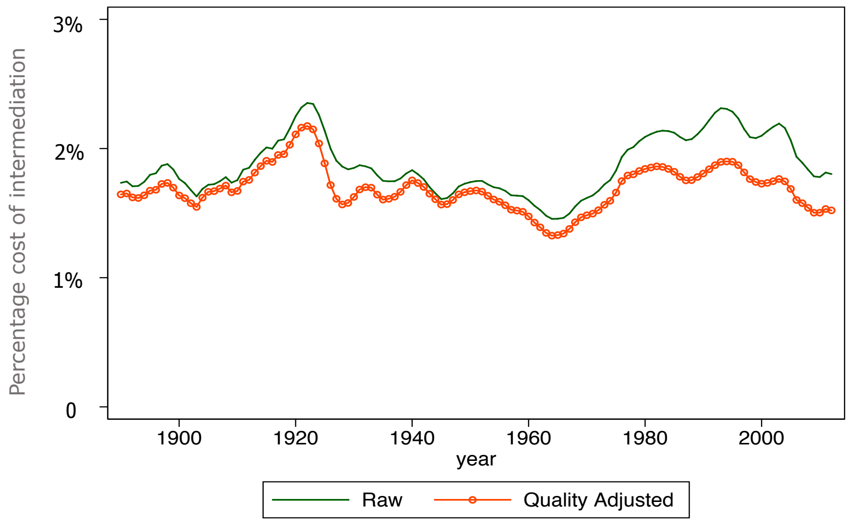

Figure 5. The cost of intermediation over time (percentage).

Moving around the rents is simply not a purposeful activity. And it is one entirely divorced from providing appropriate finance and stewardship of companies.

Similar studies on the productivity of the finance industry have been undertaken for European countries by Guillaume Bazot. They paint a similar picture. However, one remarkable difference is that *the UK seems to have a lower cost of intermediation than other nations*—albeit with little improvement over time. Properly promoted, one might think this would be a huge competitive advantage.

Let us now focus on how well the institutions of finance fulfil their purpose in providing funds and stewardship to companies.

4.2. How well do the institutions of finance provide funds?

British companies are typically funded through loans provided by banks, and through bonds and equity provided by fund managers and insurance companies [see Figure 2]. This service, if properly provided, creates huge value.

Yet anecdotally, it seems that practices have been allowed to develop which aren't delivering to purpose. For example, the scandals at HBOS and RBS suggest that those banks were lending and then abusing the fine print of the loan agreement to take control of companies, driving them to bankruptcy while talking large fees.[29]

[29] For HBOS, see Wikipedia (2019a), section 3.5 on Operation Hornet. For RBS, see Wikipedia (2019b), section on 'Allegations of asset-stripping small business customers'.

More systematically, however, one can see institutions which seem to have come adrift from their original purpose. Stock exchanges are one such example. Having emerged in the early 17th century, stock exchanges came about as a way to allow companies to raise permanent capital, typically through the issuance of shares, while allowing those holding the shares to sell them. Thus, companies were provided with permanent long-term capital while the shareholder was rewarded with a dividend while they held the share and with a cash realisation when it was sold. Trading on stock exchanges thereby created long term, permanent capital.

Today, the volume of trading on stock exchanges has increased dramatically; indeed on the London Stock Exchange the value of trading is now ten times greater (as a percentage of the market value of quoted companies), than it was just fifty years ago. Yet the number of companies quoted has actually fallen. Far from providing new permanent capital, today as much money is paid out by exchanges than is raised on them.[30]

Indeed, the trading of shares seems to have become an end in itself rather than a way to support long term investment. Take, for example, Michael Lewis' book Flash Boys, which describes High Frequency Trading (HFT). HFT effectively involves extracting information about stock market trading fractions of a second before a deal would be concluded and 'arbitraging' the trade. Using the words of Adair Turner, former chair of Britain's leading financial regulator, the FCA, it is 'not socially useful'. Some forms of HFT, if done in real time, might in fact be deemed 'front running', which is illegal.

Equity stock markets are there to provide permanent capital. Yet, as a result of the huge increase in the trading of shares, companies often consider them to be short-term. The reason may be that the fund management industry is seen to put little effort into the stewardship of the companies whose shares it own, but rather concentrates on the trading of shares to demonstrate 'outperformance'. By its nature the trading of shares is a short-term activity, it is costly, and even before those costs is, in aggregate, a zero sum game. So while some trading is important to allow companies to raise permanent capital, and allow savers to adjust their portfolios, the scale of trading in today's markets seems well in excess of what is purposeful. As one workshop participant put it, if the industry is not 'corrupt', as suggested in Figure 3, it is at least 'perverse'.

Other features of the finance industry and its institutions have similar characteristics. They are simply not focused on meeting the purposes that address the needs of savers or borrowers.

[30] Wainwright (2019).

4.3. How well do the institutions of finance provide stewardship?

By law, company directors are at a minimum required to promote the success of the company, for the benefit of the shareholders 'as a whole', whilst having regard for other stakeholders (Sec 172 of Companies Act 2006). As discussed above, the beneficial owners of most public companies are millions of individuals saving for their pensions. Therefore, promoting their benefit while having regard to stakeholders is at least a starting point for 'enlightened shareholder capitalism'.

One would think that a purposeful financial system, would work in the interests of those whose savings it manages. It would want to promote profitable purposeful growth which did not externalise costs. As we have noted, shareholders have substantial powers to do so, including the appointment of directors, and auditors and the approval of their remuneration.

But today's fund management industry is not structured to deliver stewardship. Indeed, most fund managers are not judged by the absolute performance of the companies in which they invest, be it financial, social or environmental. Rather, they are judged by their financial performance relative to other fund managers investing in a similar class of assets. Performance is measured in terms of relative performance—termed alpha—not in terms of 'beta', the performance of companies in aggregate. Yet it is beta which will ultimately be the most important in determining the outcome for the saver.[31]

This is not to say that fund managers entirely ignore their stewardship responsibilities. Blackrock, for example, has around 40 people dedicated to the stewardship of the companies in which it has invested client monies. It is one of the largest such resources of any fund manager. In 2020 Blackrock had 16,500 employees, and invests over $9 trillion in many thousands of companies, so its stewardship resource is relatively modest. Yet Blackrock would claim to be something of a leader in the field.

So the stewardship function of purposeful fund management is inadequately served. Much resource is devoted to other less purposeful activities.

5. Creating a more purposeful finance industry

The previous sections of this article have set out some characteristics one might expect from a 'purposeful' finance industry, and some reasons as to why we currently don't have such an industry. We have also considered the impact this has on the purpose of the corporation. This final section will consider how we might find ways to create a

[31] Lukomnik & Hawley (2021).

more purposeful finance industry. In particular we will look at initiatives in politics, academia and the industry itself. We will also examine the role fintech might play given its prominence in the new wave of financial institutions that are emerging.

5.1. Will fintech solve the problem?

It is clear the fintech revolution is upon us. It's the buzzword that echoes across the City as new companies emerge with leaders who do not have traditional finance industry backgrounds, coming instead predominately from the technology sector. In the UK, it is estimated there are around 1,600 plus fintech firms, with this figure expected to double by 2030.[32] With this projection comes the hope that fintech could be the driver in delivering a more purposeful finance industry.

Technology has the power to increase transparency and efficiency, reduce cost, and give the most vulnerable access to financial services. Society and businesses both stand to gain from these changes, as incumbents are challenged by the new wave of digital innovation. And it is rapidly transforming the financial services sector with mobile banking apps, robo-advisors, peer-to-peer lending services, crowdfunding campaigns and cryptocurrencies – these are all Fintech innovations.

Fintech advances are made possible through data and efficiency. Whether they form the solution to a more purpose driven finance industry is yet unclear. This is dependant not on the technology but on the strategy and motivations of those creating the business model. We cannot take it for granted that innovation will lead to customer benefit. Indeed as we have noted, the evidence presented by Thomas Philippon suggest that in aggregate, technology has made little difference to productivity over the past 130 years.

Let us consider one example: a fintech business delivering personal loans.

The core of the business model is to develop a platform that uses alternative data sources, such as utility bills and predictive information, in order to understand their customers financial lives and to assess their ability to repay. From this data, fintech companies are able to create products tailored to their customers, for example by providing loans based on cash flow rather than on collateral. This has significant advantages in opening up borrowing to those without significant wealth or assets. And as operational efficiencies increase with improved technology, costs decrease and fintech platforms can afford to serve harder-to-reach customers who need small loans, something that traditional banks won't do.

Yet the same data and efficiency advances that allow new customers to be included can just as easily allow them to be exploited. Predatory lenders can target a larger,

[32] Department for International Trade (2019).

often less financially savvy audience, providing easy access to capital that comes with lots of strings, such as hidden fees and high interest rates, leading to a cycle of over-indebtedness.

Fintech shouldn't be seen as silver bullet to solving the issue of a more purposeful finance industry. There is an 'ecosystem' that motivates the entrepreneurs, determines industry practices and ultimately shapes the business models of finance companies. This ecosystem needs to be one that encourages purpose driven activities, and allows them to flourish. In this next section, we will explore this further looking at some suggestions for reform, that would help ensure that markets, competition, institutions, incentives, cultures, regulation and training can combine to create a more purposeful finance industry.

5.2. What needs to be done to create a more purposeful finance industry?

This section explores what might be done across government, education and the industry itself to enable a fundamental shift in thinking to a more purpose driven industry. All must recognise that where markets are characterised by 'asymmetric information', it must not be assumed that the invisible hand of markets will alone deliver purposeful outcomes. Other approaches are also likely to be needed. We do not claim that these recommendations are comprehensive. Rather, they set a direction for reform, and an opportunity to begin a discussion as to how change might occur to deliver a more purposeful industry. Nor do we suggest that there is a silver bullet that will deliver the solution. In the workshop discussions of this article it was clear that the achievement of a purposeful finance industry will require the actions of many; our educators and researchers, our policy makers and regulators, and above all the participants within the industry itself. Here we make some suggestions for reforms including several suggestions that we believe are both practical, and illustrative of the sorts of positive change we would wish to promote. In the final section of the article we will focus particularly on how this fits with the larger study by the British Academy about the purpose of the company.

Recommendations for education and research

Given that this article is written for the British Academy, we might begin by looking at our education system, which provides the source of talent for the industry, and the source of intellectual capital on which the business models and practices of the finance industry are built. Be it through graduate or undergraduate studies, the financial services industry in the UK is a major employer of graduates. Finance is a popular subject, one that for many graduates is the key to securing a first step on the career ladder. Yet, when we examine the curriculum, there seems very little that examines the purpose of the industry, or even its basic functions, and how they can best be achieved.

Teaching is firmly rooted in the models of neo-classical economics. These are precisely the ones which suggest that the invisible hand of markets will alone lead to good solutions. Such a model has strengths. But it is entirely inadequate to describe how finance can best fulfil its purpose. Finance students will in time be the leaders of their industry. If they are to be purposeful, they need to learn the different disciplines that can help guide the industry to its fulfilment. Our first recommendation in delivering a more purposeful finance industry would be that **finance needs to be taught at undergraduate and postgraduate levels with an emphasis on purpose. This needs to be an integral part of the core curriculum. Academic research should similarly be encouraged to investigate purpose and how it is best realised.** This might suggest that broader disciplines, some of which we have mentioned earlier – psychology, sociology, ethics – need to be more firmly embedded in the body of knowledge which defines the finance curriculum. Given its membership, the British Academy might play a particularly influential role in fulfilling these recommendations.

Connected to this, our second recommendation focuses on the way in which professional qualifications are drawn up. Professional qualifications accredit the skills of those within the industry. They are important in delivering high standards of learning. They also hold an important role in ensuring that purpose is part of professional conduct and practice. In accrediting doctors, we take it for granted that not only do they understand the technicalities of medicine. They also commit only to work on behalf of their patient. Indeed, the Hippocratic Oath requires such behaviour. Finance professionals should similarly be able to demonstrate their commitment to delivering a purposeful service, and indeed we applaud the considerable work which has been done by professional organisations such as the CFA to embed these issues into its curriculum and qualifications. So, our second recommendation would be that **professional qualifications for the finance industry should support purpose in the same way as they do in the medicine, ensuring that those who pass these qualifications are not just technically qualified but understand and commit to the purpose of the profession they practice.** This might be associated with the introduction of a 'Hippocratic oath' for finance professionals.

Workshop participants also felt it would be helpful if all of those who use the finance industry have a basic financial education, just as those who use the health system should take some responsibility for their own health. We would conjecture that such an education might focus on those financial services which are needed as a 'utility service'; bank accounts, pensions, mortgages, business loans and insurance. Again, using the analogy with health, we do teach people about the need for a good diet, and plenty of exercise. We do not expect them to be experts in pharmacology or anatomy.

Recommendations for regulation and policy

Regulation is essential and should help the industry fulfil its purpose. Yet its practice has proved a mixed blessing. Arguments exist both for and against regulatory intervention. On the one hand, some argue that the industry cannot be trusted, others make the case against heavy-handed regulation, arguing that it is costly to both good and bad suppliers of financial services. What is clear is that regulators have never been explicit in their promotion of a purposeful financial system. So we would recommend **that policy makers and regulators seek to adopt the lens of purpose when looking at new rules.** Before new regulation is adopted, they should be explicit about their 'theory of change'; how the regulation in question will create a more purposeful industry. They should regularly test whether their assumptions have proved correct, and learn from those assessments. In particular, they should note that changes in one part of the financial services industry have knock-on effect to others. Regulators need to be explicit about this. If, for example, accountancy standards are changed so that they are no longer based on the principle of 'prudence', then the regulators of banks will need to take this into account in determining appropriate solvency levels. If the promises made to savers must be guaranteed, that this will restrict the risk capital available to companies.

We should also **revisit the Terms of Reference of our regulators so that they have an adequate set of tools to ensure financial markets are purposeful.** Many regulators have a remit that tends to reflect the assumption that markets and competition are adequate policy leavers to deliver good outcomes.[33] As we have seen, this is not a safe assumption. So, where it is inadequate, they might be offered further powers which, used more sparingly, can allow the industry to fulfil its purpose better. This in turn means they need to create an understanding of what purpose is, promoting this understanding amongst other industry participants. They need a mindset which is based on purpose and **metrics** assessing how well the financial system and financial firms are fulfilling it.

This may lead to the exploration of new policy approaches. For example, today, risk weighted bank capital is almost exclusively based on statistical measures. (Small business lending is the one exception.) While such measures are important, they may well be encouraging purposeless trading. Might regulators judiciously encourage purposeful and discourage purposeless activity? Another example would be stock exchanges. We mentioned earlier that, despite huge increases in trading, the amount of capital being raised is reducing. Some suggest that much of this trading is, in aggregate, purposeless. Yet might this not suggest there could be room for institutions, taxes

[33] The FCA, for example, is charged with protecting consumers, promoting effective competition and ensuring market integrity.

or regulations to discourage such over-trading? We note this is not necessarily the role of the regulator. The creation of the IEX stock exchange in the USA, which has introduced short delays on trading to address the costs paid by bona-fide market users to High Frequency Trading (HFT), required no new action from regulators.

We have noted that, if markets were working perfectly, and everyone had full information, they would ipso facto fulfil their purpose. Current arrangements, however, allow those who manage money to profit at their customers' expense. There is a standard governance mechanism to respond to this issue. That is to **embed fiduciary duty throughout the chain of agents who manage money.** So for example, a pension trustee owes a fiduciary duty to members. Even a company director owes such a duty through Section 172. However, other financial intermediaries typically only need to fulfil their contract. They do not always need to act always in the best interests of the person whose funds they are managing, leave alone considering wider societal impacts. We should further clarify and promote fiduciary duty, so that it does not ignore externalities, or encourage free riding. Where such duties do not already exist, trustee-like bodies could be created and empowered. The creation of Independent Governance Committees, and the recent discussion of extending their powers, could be a case in point.

Ensuring that a legal obligation exists to act in good faith in the interest of others would allow the question of purpose to be central to the development of strategy and innovation. It would allow us to create the institutional and governance structure to allow markets to work in a benevolent fashion.

We should also be sure that **appropriate institutions are in place to ensure that purposeful financial services can be delivered**. For example that it is possible for citizens to save for a 'pension', meaning an 'income in retirement'. Today, outside the public sector, and despite the fact that we have an effective national system of pension savings, we have no effective system for pension drawdown. Similar observations might apply to the provision of long-term funds to private companies. Until the 1980s 3i (ICFC) had a network of local offices providing such funding. Inexplicably this valuable service was abandoned, and is now having to be recreated through the British Business Bank.

We should insist that the prerequisites for the efficient operation of markets are in place. For example, today, investment funds do not declare to those who are saving, the full costs of doing so. Markets don't work if customers are unaware of how much they are charged.

Recommendations for participants in the industry

The pursuit of purpose will change many aspects of finance industry practice. Just as the British Academy advocates for the definition of company purpose, so there is a need to define the purpose of companies within the finance industry. Indeed the need may be greater in finance since the purpose of its institutions may not be so clear, either to participants or to other stakeholders. We hope that our definition of purpose might be helpful in framing that discussion for companies within the finance industry. In particular to note that they are part of a system to serve the outside world with specific services. Approaching company strategy in this way may be challenging for the industry. The evidence suggests that much current activity is not focused on purpose. But it is challenging in a positive sense too, since many purposeful demands from the finance industry remain unmet. We noted above the inadequacy of UK pension provision. With around £3 trillion saved to provide pensions, that is surely a huge opportunity. A similar thing could be said about the inadequacy of financing for small companies. So there are big opportunities that open once purpose becomes the starting point for company planning.

Companies themselves will discover most of these opportunities, with benefits for their workforce, suppliers and society. But let us give just one illustration of how a finance industry more focused on purpose could help create purposeful companies.

Markets are unlikely to work if those who participate in them are given the wrong incentives. As a recent study by NESTA demonstrates, corporate directors are frequently given short term performance targets, despite the insistence by their investors that they wish them build purposeful companies for the long term.[34] The irony is that it is those same investors who approve the incentive packages offered to company directors. So it is entirely within the power of the investment industry to ensure that corporate directors receive incentives which will drive them towards purpose and long-term value. No regulatory action would be required.

Many other recommendations could be made with the aim of creating a more purposeful industry. We believe that they, and many more positive reforms on policy and practice would emerge if we were simply to be more informed and explicit about purpose in the conversations and debate around and within the finance industry. As we discussed earlier in this article, the purpose of finance is a topic which has seen little debate. We would argue, that if academics, think tanks, policymakers, those developing strategy within our financial services companies started by asking the question ‘Does this activity achieve a purposeful outcome?’ we would see a shift, in institutions, regulations, culture and markets that would embed itself into the way in which our finance industry operates.

[34] NESTA (2019).

One reason for this gap is lack of information. There is no comprehensive study that has asked the populace what they would like from the finance industry. There is little reliable evidence on how the finance industry is spending its money, and the services which derive from such spending. In other words there is a huge need for basic research on the services we should expect from a purposeful finance industry. The authors would suggest that this might best be discovered through citizen juries, and that it might well reveal the 'utility services' which need to be delivered. But amazingly, despite its consuming such a large proportion of our GDP, this basic evidence is lacking.

5.3. The purpose of finance and the purpose of the corporation

Our argument has been that these reforms to create a purposeful finance industry will assist in creating purposeful companies. A finance industry managing the citizen's capital would invest for the long term; it would use the power of diversification to allow companies to take (idiosyncratic) risk. It would encourage the raising of new funds—both for permanent capital through equity, and through bonds and other loans. As regards stewardship, equity funds would still encourage companies to seek returns, but would be clear that stakeholders needed to be treated fairly, and that companies should not profit through the externalisation of costs. They would actively use their shareholder powers to promote social and environmental outcomes, as well as financial ones. Indeed one can see much of this taking place in scores of initiatives such as the Principles For Responsible Investment, or Climate Action 100+.

But although much useful activity is taking place, and many worthy words spoken in support of purpose, today's finance industry can hardly be deemed purposeful. If it were reformed, along the lines we are suggesting, how might that affect its ability to respond to the challenges presented in Principles 7 of the Principles for Purposeful Business, and how might it impact on some of the other recommendations made in that paper?

Principle 7 aims to create long-term sources of finance, and for equity holders to encourage a long-term perspective: **'Corporate financing should be in a form and duration that allows companies to fund more engaged and long term investment in their purposes.'**

The reforms we have suggested would support this principle, and its objective of encouraging long term investment. Concerningly there is a gap in finance for smaller private companies seeking risk capital. To address this may require new institutions or bolstering of existing ones, such as the British Business Bank. And as we have noted these institutions themselves would benefit from being explicit about their purpose. Similarly banks and other financial institutions, their operations underpinned by fiduciary responsibility, and their regulators being explicit about purpose, should offer more consistent long term funding.

As regards regulations and taxes, we have suggested that there may be many opportunities to promote modest changes which can have significant effects; from the calculation of risk weighted assets to the introduction of delayed trades on stock exchanges. Our suggestion is that, rather than a wholesale reform, these small changes could have a profound effect. Indeed unless attention is paid to these issues major reforms may founder.

But perhaps the most significant effect of moving towards a purposeful financial system will be its effect on stewardship. The reforms we have proposed will tend to discourage the trading of shares, and encourage investors to be more active in the stewardship of companies. For example, when the Hermes Principles were written, they were an explicit attempt to incorporate stewardship as a fiduciary duty for fund managers. As part of the exercise of those principles, Hermes undertook to support well run companies facing a hostile takeover. In our workshops, some raised the question of whether the fear of hostile takeovers dissuaded managers from pursuing purpose. In effect Hermes addressed this concern. Within a purposeful system these sorts of long-term relationships between investor and company might tend to become the norm.

Other recommendations in the 'Principles for Purposeful Business'

There are however certain recommendations in the *Principles*, where the mechanism for achieving them might merit discussion. Shareholders will be likely to support purposeful companies, as we have noted in Section 4. However, they are likely to be concerned about legal changes which involve a loss of accountability. Indeed, if directors cannot be held to account, it may be difficult for companies to raise equity capital, since equity has few other contractual rights. There is however considerable progress which could be made towards purpose without changing current laws. We have already noted that Section 172 (1) of the Companies Act requires directors to promote the success of their company for the shareholders 'as a whole', as well as having regard to stakeholders. Fiduciary duty would suggest that the shareholders would be millions of individual savers, and stakeholders' interests should also be served. However, this section of the Companies Act is unenforceable since the directors' duty is owed to the company itself. It cannot be used by those whose rights it aims to protect. **Stakeholders and shareholders alike need an affective remedy if the rights they enjoy under the law are abused. There needs to be some enforcement mechanism for the duties of directors.** Indeed, many would argue that the directors of companies who have behaved badly (e.g. Sports Direct and BHS) were in breach of the law. Indeed, even if purpose was more explicitly incorporated within company law, it is unlikely to have very much effect unless it is enforceable.

Of course, it is perfectly possible under current law to entrench purpose within a company's statutes, if founders, or subsequent shareholders wish to do so. This involves the use of Section 172(2). But this provision is hardly ever used. One way to do so might be to **encourage those private companies which provide public services to adopt the provision offered by Section 172(2)**. This might be a more effective way to ensure they operated in good faith, than creating ever more regulations. This might be particularly germane for utility companies, and other highly regulated industries, including finance.

5.4. Recommendations for future activity

We are deeply indebted to the British Academy for supporting this work around the purpose of finance. In this article, we have set out a series of practical recommendations which will help achieve a more purposeful finance industry. These recommendations cover a very broad field, from the way we teach finance, to the duties of finance practitioners; from the terms of reference of regulators, to the design of our financial institutions. We do not believe that this is a comprehensive list. Nor do we believe they will be achieved overnight. However, we do believe that these are practical suggestions, all of which build on existing initiatives which aim to promote a purposeful system.

In particular, we feel that two areas of further work and research stem from this article. The first might examine what purpose looks like in specific financial institutions—banks, insurers, stock markets and the like – and that each might seek to define its particular purpose. We note the comments made at the workshop that this would help to provide a further level of granularity of what purpose means within the industry and the actors and institutions within it. The second area is around what model of change might look to drive change within the industry and its various sectors. Within this, an analysis of the likely costs and benefits of each of these recommendations would provide a useful way in which to debate how to create a shift towards a more purpose driven industry.

We hope that this article will encourage more research, debate and discussion around the purpose of finance. It is desperately needed. At present there is an active debate about the purpose of the company. But debate about the purpose of the financial system is all but absent. A focus on purpose would result in practical changes to our education system, our legal and regulatory environment, and to the practice of finance. We do not pretend that this is a blueprint for perfection. However, it sets a direction. And by taking this path, the financial system will be better able to support the emergence of companies which are truly purposeful. We look forward to working with the British Academy in achieving that goal.

Acknowledgements

The authors would like to thank the British Academy for their kind support in commissioning and supporting the work in this article. In particular, we would like to thank Professor Colin Mayer and Henry Richards in commissioning and guiding the writing of this article. We would also like to thank the Pensions Insurance Corporation for their initial support in 2016 in helping to establish the first parts of this research into the Purpose of Finance and the sponsorship of that work. Finally, we would like to thank all those who attended the workshops at the British Academy which reviewed this article and provided the authors with insightful support in its revisions.

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Appendix 1. Stakeholders consulted

Through 2017 to 2019 we have held a series of discussion groups with a variety of stakeholders detailed below. These have formed part of our research; asking others how they define ‘the purpose of finance’. We have listed these below.

1. Four practitioner focused meetings of approximately 20 members from financial institutions. The majority of those participating have been senior level leaders within these organisations, most of whom are tasked with thinking about the strategic direction and activities of the firms they represent. Some participants represented global financial organisations but the majority have been from the UK, and London based.
2. Larger forums with multiple stakeholders from a variety of industries and roles connected with the finance industry. In total, we have had around 300 stakeholders attend these forums where our research has been presented and discussed.
3. Various conferences, presentations and panel discussions around the theme of the Purpose of Finance. These have included conferences focused on responsible investment as well as more general conferences about the finance industry.
4. Presentations to the Bank of England, and the Financial Conduct Authority.
5. Presentations to the All Party group on Inclusive Growth, and the OECD Parliamentarians Network
6. Academic audiences within the Global Research Alliance for Sustainable Finance, Cambridge University, London Business School and within the work stream of the Future of the Corporation at the British Academy.

Appendix 2. The methodology used for the literature review research

Our review in 2017 encompassed looking at the following search terms through 'Google Scholar'. We review the literature and the key studies that were found on the following topics in the main body of this article.

- The purpose of finance
- The function of financial markets
- The existence of financial intermediaries
- The purpose of banks, insurers, and pensions

In 2019, using the above search terms we reviewed this literature, and in addition surveyed the following 10 journals considered to be the highest-ranking journals in finance, using the worldcat search engine. The conclusions of our findings are in the main body of this article.

1. *Journal of Finance*. Published by Wiley. The official publication of The American Finance Association, which publishes English-language research in all areas of finance.
2. *The Review of Financial Studies*. Published by Oxford Academic. Covering both theoretical and empirical work in finance. Argued to cover the most relevant studies in Finance.
3. *Journal of Financial Economics*. Published by Elsevier. Covers the areas of capital markets, financial institutions, corporate finance, corporate governance, and the economics of organisations.
4. *Journal of Accounting and Economics*. Published by Elsevier. Focuses on the interface between economic theory and the practice of accounting.
5. *Journal of Financial and Quantitative Analysis*. Published by Cambridge. Covering theoretical and empirical research, in the topics of corporate finance, investments, capital and security markets, and quantitative methods.
6. *Journal of Banking and Finance*. Published by Elsevier. Covers research on Financial institutions and the system in which they operate
7. *Journal of Money, Credit and Banking*. Published by Wiley. Covers broad areas of money, banking, credit markets, regulation of financial institutions, international payments, portfolio management, and monetary and fiscal policy.
8. *Journal of International Money and Finance*. Published by Elsevier. Covers international monetary economics or international finance.
9. *Journal of Business Finance & Accounting*. Published by Wiley. Covers topics in accounting, corporate finance, and corporate governance.
10. *Journal of International Financial Management and Accounting*. Published by Wiley. Covers international aspects of financial management and reporting, banking and financial services, auditing, and taxation.

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To cite the article: Pitt-Watson, D. & Mann, H. (2022), 'The purposeful corporation and the role of the finance industry', *Journal of the British Academy*, 10(s5): 125–161.
https://doi.org/10.5871/jba/010s5.125

Journal of the British Academy (ISSN 2052–7217) is published by
The British Academy, 10–11 Carlton House Terrace, London, SW1Y 5AH
www.thebritishacademy.ac.uk

Journal of the British Academy, **10(s5)**, 163–207
https://doi.org/10.5871/jba/0010s5.163
Posted 26 August 2022

Principles of purposeful business: illustrative examples

Charles Ebert and Victoria Hurth

Abstract: In this article, we identify examples of business practices currently or recently implemented that illustrate one or more of the *Principles for Purposeful Business* as defined by the British Academy's Future of the Corporation programme in 2019. We draw on existing networks and sources to identify examples which are predominantly large publicly listed corporations where we feel some of the greatest challenges to adopting the principles are likely to be. The examples are drawn from companies which generally express a purpose, though their inclusion in this article does not mean the company is necessarily a 'purposeful business'. We draw on insights from stakeholder interviews, academic writings, practitioner articles, company reports, press releases, and legal documents from government sources. Our findings illustrate some of the types of practices that may be required to implement the *Principles for Purposeful Business*. These descriptive examples can be taken as starting points for further exploration, analysis and research.

Keywords: Organisational purpose, purpose-driven, governance, regulation, corporate law, ownership structure, financing.

Note on the authors: Dr Charles Ebert is a postdoctoral researcher at Colorado State University, studying corporate purpose, meaning at work, and company performance. Dr Victoria Hurth is an independent academic, and Visiting Fellow, Cambridge University Judge Business School.

Introduction

In recent years, support for the idea of purposeful business has been growing rapidly, both in academic and business circles. This reflects the range of increasingly clear issues facing the wellbeing of life on earth (Dearing *et al.* 2014; Steffen *et al.* 2015). While different kinds of organisations and businesses such as charities and governmental institutions and have placed positive outcomes for others at the heart of their operating model, large publicly listed institutions are also now starting to address wellbeing outcomes of people and planet as their core strategic directive (e.g., BT 2015; Jones 2018; Unilever 2020; Walgreens Boots Alliance 2020). In addition, support for the advancement of purposeful business now exists through consulting services, rankings, and policy reports that help companies be more purpose-driven (Radley Yeldar 2016; Game Changers 2017; Ebert *et al.* 2018; Boston Consulting Group 2020; Gast *et al.* 2020; PricewaterhouseCoopers 2020; Schaninger *et al.* 2020;

Table 1. Replication of the *Principles of Purposeful Business* from the British Academy

Principle Category	Principle
1. Company law	Corporate law should place purpose at the heart of the corporation and require directors to state their purposes and demonstrate commitment to them.
2. Regulation	Regulation should expect particularly high duties of engagement, loyalty and care on the part of directors of companies to public interests where they perform important public functions.
3. Ownership	Ownership should recognise obligations of shareholders and engage them in supporting corporate purposes as well as in their rights to derive financial benefit.
4. Governance	Corporate governance should align managerial interests with companies' purposes and establish accountability to a range of stakeholders through appropriate board structures. They should determine a set of values necessary to deliver purpose, embedded in their company culture.
5. Measurement	Measurement should recognise impacts and investment by companies in their workers, societies and natural assets both within and outside the firm.
6. Performance	Performance should be measured against fulfilment of corporate purposes and profits measured net of the costs of achieving them.
7. Finance	Corporate financing should be of a form and duration that allows companies to fund more engaged and long-term investment in their purposes.
8. Investment	Corporate investment should be made in partnership with private, public and not-for-profit organisations that contribute towards the fulfilment of corporate purposes.

This table replicates the *Principles of Purposeful Business* published by the British Academy (2019). Most are self-explanatory, although it should be noted that Finance was understood in a broad fashion for this article.

Blueprint for Better Business 2021; Contexis 2021; Neighbourly 2021e; British Academy 2021). This trend is only likely to increase along with rising societal pressure for solutions to social and environmental issues (Hollensbe *et al.* 2014).

Despite this increasing interest in organisational purpose, there remain gaps in knowledge around how to apply concepts of purposeful business such as that set out by the British Academy: *'producing profitable solutions for the problems of people and planet, and not profiting from creating problems'* (British Academy 2018). In particular, publicly listed companies that have been oriented towards prioritising shareholder interests face numerous challenges to becoming more focused on purpose. To address such impediments to purposeful business, the British Academy Future of the Corporation programme set out eight *Principles for Purposeful Business* (British Academy 2019; see Table 1).

This article presents a selection of examples of practices currently or recently implemented by firms, and attempts to illustrate the *Principles for Purposeful Business* as defined by the British Academy's Future of the Corporation programme. Ten illustrations are provided. Seven of the illustrations involve publicly listed companies, which the authors view as the most challenging context for the implementation of the principles. An additional two illustrations are privately owned firms – one relatively large and one relatively small. Finally, one illustration is a company limited by guarantee. This illustration provides an interesting example of a joint venture between governmental and insurance entities, which can be informative and instructive for other organisational firms seeking a way forward in their purpose journey. In aggregate, the samples focus on large shareholder owned companies but offer some variety and breadth of scope, reflecting the relevance of organisational purpose beyond publicly listed companies. Table 2 summarises which examples provided in this article relate to each principle.

The next sections cover the methodology used in the collection and analysis of examples used in the article, due diligence on the examples provided, and a critical analysis of the companies in the example set. The subsequent section presents each of the specific examples chosen including a summary description of the company, followed by subsections that describe how the practices observed in the example address the relevant *Principles for Purposeful Business* set out in Tables 1 and 2.[1]

[1] In general, subsections are ordered in line with the ordering of the principles in Table 1. However, the ordering of the subsections is sometimes altered to improve the narrative flow of the examples.

Table 2. Examples of companies described in this article implementing practices associated with the *Principles for Purposeful Business*.

Principle Category	Types of associated practice	Examples
1. Company law	Companies incorporate a purpose into their articles of incorporation.	• Anglian Water • Neighbourly
2. Regulation	Directors and controlling owners of companies are held to account for the achievement of the purpose.	• Anglian Water • Biffa • Flood Re • Interface
3. Ownership & Governance	Companies make purpose a central aspect of their annual reporting and demonstrate how their ownership is aligned with delivering the purpose.	• Anglian Water • Biffa • Interface • Quilter • Anglo American • BT
4. Measurement & Performance	Companies adopt non-financial metrics to measure impacts on stakeholders that either directly or indirectly relate to the achievement of the purpose.	• Anglian Water • Biffa • Flood Re • Interface • Natura • Pearson • Quilter • Anglo American • BT
5. Financing & Investment	Companies shift financing arrangements to allow faster, higher quality delivery of the purpose, and partner with others to achieve shared purposes.	• Anglian Water • Biffa • Flood Re • Neighbourly • Interface • Natura • Anglo American

This table lists the companies considered in this article that implement some of the practices associated with the *Principles for Purposeful Business*. Financing is interpreted in this report in the broad sense, including not only raising funds in terms of loans, bonds or share capital, but also in terms of the how the company is financed through the business model.

Methods

The selection criteria for the examples in this article follow best practice for purposive sampling and exploratory research (Dexter 2006). We looked for organisations that self-declare as being engaged in the pursuit of organisational purpose and were also understood by peers to be active pursuers of purposeful business. This does not mean that the organisations had achieved the goal of being completely purpose-driven, but that they were conscious and active in their pursuit – or at least were perceived to be. In addition, we sought out firms that appeared to demonstrate progress toward at least one of the eight principles offered by the Future of the Corporation.

Our sampling focused predominantly on large, publicly listed institutions or those supporting them, which is where we believe the largest hurdles to purposeful business exist and yet where we observe notable transition efforts. In line with this reasoning, and perhaps controversially, we included an example from one of the most challenging sectors – mining. The mining industry has a chequered past (Chepkemoi 2017; National Geographic Society 2020; Stewart 2020), and thus an illustration of purposeful business in the mining industry is an attempt to 'shine a light in the darkest room'. In addition, and as a result of our snowballing sampling approach, we included three examples of different organisational forms, namely two privately owned firms and one firm limited by guarantee. These examples were included due to their reputation for being on a purpose journey and to reflect the applicability of purpose beyond publicly limited companies. Of course, we recognise other ownership structures exist and are important in today's business environment (co-operatives, mutuals, trusts and other ownership structures and do not fall under any particular category). Our view is that the illustrations provided here, although partial, will be of benefit to such organisations as well. We also did not focus on trying to disaffirm the assumption – i.e., we did not seek data on our sample firms that showed they were not purpose-driven in some areas, even while they tried to be purpose-driven in others. We assume such examples are prevalent as organisations grapple with purpose, and that at this stage, there is value in taking a methodological approach which transparently highlights positive examples.

To begin the search process, we drew on the knowledge of two professional services firms that have experience in this area (see similar methodology in Challagalla *et al.* 2014). Both firms specialise in helping organisations pursue purposeful business practice and have worked with large scale international corporations to develop organisational purpose. Based on suggestions from these corporations, we continued a 'snowball' sampling approach, reaching out to firms within our interviewees' networks that fit our sample frame. We then supplemented this initial search with examples of relevant firms known to the research team, who were experienced in researching purpose-driven organisations, or through other published material from academia or publicly available analysis. Finally, we reached out to known relevant informants from a series of panel discussions on purposeful business held by the Future of the Corporation. In aggregate, we conducted a total of 32 interviews with 35 executives across 26 companies, choosing 10 that offered the most complete illustrations of the principles.

To supplement interview data, we conducted independent research on existing practitioner artefacts (communications, project documents, etc.) and archival data. Such supplementary data adds to and corroborates these interview findings (see Strauss & Corbin 1998; Challagalla *et al.* 2014). This stage of the research process involved primarily the investigation of company legal records, annual reports, media articles, and published writings from the organisations or professionals in the field. Cases were then developed as a combination of findings from extant artifacts and interviewee comments.

While we judged the chosen methods as sufficient for the objective of this article, it is important to note the limitations with this approach to sampling and data collection. As a purposive sampling procedure, our sampling approach does not lend itself toward identifying a representative sample of a population. Rather, this sample selection method is designed to identify members of a specific group (in this case, of firms that are pursuing purposeful business principles). Moreover, in a snowball sampling procedure, the nature of the sample is influenced by the network of the first few interviewees. The initial interviewees are the link to the rest of the interviews, and their connection to the phenomenon in question is paramount to obtaining an ideal sample. The two professional services firms that acted as the start of the sampling procedure are fully embedded in the network of firms pursuing organisational purpose, and this speaks positively to the quality of the sample. In addition, both firms maintained connections to publicly listed companies who were pursuing purposeful business approaches, which was a focus for our search. Still, these positive qualities do not guarantee the sample contains the most purpose-driven companies or the best exemplars of purposeful business activity. Indeed, other organisations may have more fully developed purposes and be more impressive in their accomplishments but may simply not be in the network that we explored. In addition, our method is primarily the collection post-hoc analyses by particular individuals from a specific point in time. Hence our cases are not able to tell us anything about future direction and we are unable to ensure the absolute validity of the historical opinions of those we interviewed. The goal of our example selection was to identify if there were self-described, hence subjective, examples of purposeful activity that illustrate the practices associated with the *Principles for Purposeful Business* as outlined in the Future of the Corporation's report.

Due diligence and critical analysis

To enhance the validity of the examples chosen and the practices detailed by our informants, we undertook due diligence efforts to assess whether the information relied on was credible, and, via a holistic analysis of the company, to check that the company is not being portrayed inaccurately in relation to its purpose journey. To address the first concern, we sought out (as we elaborate upon in this section) sources of information that are traditionally understood to be more resistant to inaccuracies (i.e., where public scrutiny and potential negative ramifications of being untruthful would motivate against offering disinformation). Such sources, while likely focused on positive company action and absent of damaging information or description of difficulties and trade-offs in firms' purpose journeys, are more likely to be defensible by the companies in question. We also gathered information from a variety of sources which creates a triangulation of data. Additionally, we sought primarily current examples and activity.

Our additional data sources that supplemented our interview data can be broken down as follows. Where possible, we supplemented primary data from the senior company informants with company information collected from published academic articles and research reports (approximately 2% of citations within the examples) and from government repositories (again approximately 2%). However, the recency of company activity often means that these resources are unavailable. We therefore relied upon other information from the companies such as press releases (approximately 10%), annual company reports (approximately 12%), other official company reports (approximately 9%), and other forms of public firm communication (approximately 38%). With varying levels of probability and magnitude, official company communications can threaten brand reputation if the information is found to be false. Therefore, while we also know that such information may be unevenly positive regarding the company, what is reported has some level of reliability. Finally, the researchers utilised reports from well-respected practitioner news outlets (approximately 26%). Overall, we believe that the credibility and diversity of the sources of information used supports the validity of the examples in this article. Still, we recognise there will always be an element of subjectivity and partiality in how the practices are understood by data sources as outlined in the limitations detailed above.

Regarding the second role of due diligence – establishing a holistic view of the organisations used in this article – it is important to note that none of our examples of purposeful business come from fully purpose-driven companies that have 'completed the purpose journey'. Rather, all our example firms have areas they could improve upon in terms of addressing the proposals of the Future of the Corporation and in pursuing purposeful business more generally. Moreover, our sampled firms were deliberately chosen to span different stages of their journey of (1) intention to become purpose-driven and (2) the degree to which the ability to pursue purpose-driven objectives is embedded in the organisation. Indeed, we considered it a positive characteristic of our sample that the included firms were at diverse stages in their development towards becoming more purposeful business. Moreover, we consider it beneficial that we found companies in a diverse range of sectors, including some sectors where the introduction of purposeful business is considered quite difficult (e.g., Anglo American in the mining sector)

Among the examples in this article, Neighbourly and Flood Re were formed as purpose-driven organisations from the outset – in other words they state that their purposeful reason to exists drove the organisations inception and has driven their decision-making over time (Flood Re 2016; Companies House 2021). Similarly, Interface started transforming its business to being purpose-driven decades ago and can be observed as achieving a relatively high level of integration of its purpose into its activities and strategy. Other examples, such as Anglian Water and Biffa, do not have as long a history of integrating an organisational purpose into the company, but are public utility firms in highly regulated industries that are set up to provide a public service, and so could be considered to have more favourable conditions or incentives to transform towards purpose. However, it is not yet clear to what extent these influences affect the range of efforts they are making toward integrating organisational purpose into their business models.[2] BT, although similarly having public service roots (a publicly owned company until 1984) and having publicly committed to purpose previously, has just recently developed a new purpose (BT 2021a). Anglo American can be seen as being at the very beginning of its journey. While it has made major actions in the direction of its purpose, it faces an upward battle following a history of controversial activity (Philip Mattera 2013) within an industry that is generally seen as problematic for social and environmental wellbeing (Chepkemoi 2017; National Geographic Society 2020; Stewart 2020). Anglo has stated that they now have acquired a very defined sense of responsibility and purpose and recognise business has to be an integral part of addressing the big challenges facing society (CompanyHistory.com 2013). Our case study shows progress in respect of its purpose-driven ambitions in specific areas, notwithstanding inaction that might be occurring in other areas of activity.

The remaining example companies (Quilter, Pearson, Natura & Co) have unique aspects in their origin or approach to purposeful business that makes their purpose-journey more difficult to characterise. Quilter was originally part of a larger company, and their separation was part of a series of changes that occurred right before the firm adopted a purpose-driven approach. Their purpose coincided with this separation and refocusing of their business model and is now quite different than it was before. One could argue their purpose is new but significantly integrated in comparison to some other members of the sample. Natura & Co is a compilation of companies, all with aligned purposes that pursue a broad benefit to society. Both the

[2] As the example in the article outlines, Anglian Water has made significant efforts to incorporate its purpose into its business model, including incorporating the purpose into the company's articles of incorporation (Anglian Water 2019a). Biffa only articulated its purpose in 2019, but our research of their activity indicates an impressive pursuit of purposeful activity even before the articulation of an organisational purpose. See the example of Biffa in this article for more information.

parent company and its sub-brands all declare that they are focused on purposeful business activity, but classifying the company as a whole is difficult due to the individual journeys of its sub-brands. Pearson has a declared purpose that it has been pursuing for many years (education), but recently developed an 'efficacy' agenda regarding the evaluation of their 'products and services in order to earn learners' and educators' trust through transparency, rigorous research, and relevant resources'. (Pearson 2021a). This change, which happened in the early 2010s, has provided new focus for the company.

Given the above summary, we find it apparent that the sampled companies cover a range of stages in the development and implementation of purposeful business practice. The following sections provide further detail on each company, and discuss how each company aligns with the proposals of the Future of the Corporation.

Example 1. Biffa

The company

Biffa is a waste management company in the UK, focusing on a range of waste management operations including waste collection, reuse, recycling, treatment, disposal and energy generation. Currently, Biffa spans 95% of UK postcodes (Biffa 2020a) and is the second largest waste management company in the UK in terms of total revenue (Tiseo 2021).

In 2019, Biffa established its purpose as: 'We're here to change the way people think about waste' (Biffa 2021a). Implicit in the purpose statement, and elaborated by the firm in strategy and communications, is the understanding that the way people think about waste would be changed in ways that improve societal outcomes of waste management. The connection between the purpose and solving problems to improve long-term wellbeing is indicated clearly in the firm's 2020 annual report:

> *We believe our 8,000+ team can lead the way in achieving a sustainable future for the UK, helping to change the way people think about waste.*

Biffa's focus on changing the way people think about waste is also particularly transformative in spirit, focusing on influencing both internal and external perceptions of what waste is and what it can be used for. Biffa has built its overarching strategy to achieve the purpose into its purpose statement, hence 'changing the way people think about waste' guides Biffa's innovative approach to helping achieve a sustainable future for the UK. Cory Reynolds, Corporate Affairs Director for Biffa, captures the need for innovation in a recent interview with the authors, while describing developing waste management techniques:

> *When you think about things like chemical recycling, or what's called pyrolysis where you can break down the bonds of things like plastic film, which are hard to recycle and hard to develop a quality product from at the moment. That's something where there's a lot of innovation happening. It has to happen. You need the innovation to drive the broadening of the recycling waste streams.*

Two of the firm's core strategies are directly tied to the firm's pursuit of its purpose, (1) developing services and infrastructure, and (2) optimising systems and processes (Biffa 2020a). Developing new services and infrastructure for removing waste will increase the amount of waste that can be collected and possibly introduce new ways of treating or using waste. Optimising systems and processes will reduce the environmental costs of operations.

Biffa's overall strategy covers three newly defined areas that specifically target different approaches to its purpose. Cory Reynolds explains these:

> *One area is specialist services, which is about customers fulfilling sustainability ambitions and providing more bespoke solutions. So that includes surplus redistribution, integrated resource management, and hazardous waste services. … The other two areas are collection and resources-and-energy. So collection, … that's really about finding the most efficient, low-carbon waste and recycling collections related to industrial and commercial municipal and household customers. … And the last area is Resources-and-Energy. And that's really about maximising the recovery of energy and resources from waste, and developing/investing in our leading waste treatment process and capabilities.*

Principles 2 and 3: Regulation + Ownership & Governance

As stated in the firm's 2020 annual report, the board is, *'responsible for setting the Company's purpose and values and ensuring these are aligned with the Group's culture'* (Biffa 2020a), which is directly aligned with the 2018 Corporate Governance code. The board delivered on these responsibilities first by establishing the current purpose in 2019, and then by monitoring the alignment of the company's culture with the purpose on an ongoing basis. To monitor cultural alignment, the board relies on a number of measures spanning employee engagement surveys to health and safety measures.

Finally, the company's executive directors are partially incentivised to help the firm pursue its purpose via annual bonuses that are tied to (1) the pursuit of the firm's three core strategies (two of which are directly tied to the firm's pursuit of its purpose) and (2) particular environmental outcomes that are in line with firm's purpose (Biffa 2020a). Environmental KPIs that underpin the purpose and currently exist within the director incentive structure include tons of waste processed, tons of waste collected, and CO2e (carbon dioxide equivalent) emissions reduction. These KPIs, along with other KPIs focused on safety and sustainability, comprise 5% of the annual bonus for directors. Strategy execution, which relates to implementing plans to pursue the aforementioned KPIs, comprises another 5% of the annual bonus.

Principle 5: Financing & Investment

One method by which the company is investing to deliver on its purpose is through acquisitions. This is a strategy that the company is familiar with, having integrated 45 companies into the business since 2013 (Biffa 2021b). Below are two examples of purpose-aligned collaborations and acquisitions:

- In 2021, Biffa acquired Company Shop Limited (CSG), a company that redistributes surplus commercial food and household products that would otherwise become waste (Biffa 2021c). Cory gives an overview of the company's model and its connection for proper handling of waste.

  > *What CSG do is they take produce that would otherwise be waste, but it's from the factories, it's from production. … So, when there's been a mistake in labelling, or when something's been mispackaged. … CSG have the infrastructure, the factories, the re-labelling plants, where they can make those things compliant.*

  Once CSG makes the previous waste compliant, the product is sold at discounted prices to essential workers and in-need groups. The end result is that waste is reduced and people have more food/household products.
- In 2020, Biffa acquired Simply Waste. The acquisition allowed the firm to reduce its carbon output during collection, while also improving the customer proposition (Biffa 2020b). Therefore, the acquisition not only allowed the firm to pursue its purpose, but also to be more profitable while doing so.

In addition to acquisitions, the firm invests through collaborative actions with its customers, NGOs, and other corporations (Biffa 2021a). Below are some select purpose-relevant collaborations that the firm has recently pursued with external organisations since the development of its purpose:

- In 2020 Biffa reached financial close on two joint ventures with Covanta Holding Corporation (NYSE: CVA) and Macquarie's Green Investment Group. These ventures involve the creation of two waste-to-energy conversion facilities, the Newhurst Energy-from-Waste ('EfW') Facility in Leicestershire, and the Protos EfW facility in Cheshire. The Newhurst EfW facility will receive around 350,000 tons of waste annually and will generate enough low-carbon energy to power approximately 80,000 homes (Covanta 2020). The Protos EfW facility will receive around 400,000 tons of waste annually, and will generate enough low-carbon energy to power approximately 90,000 homes (Biffa, 2020c).

These two joint ventures turn waste into an energy source and simultaneously reduce the amount of waste that is exported from the UK. Converting waste into energy in the UK reduces the cost of waste transportation, increases energy output, and decreases carbon footprint. Simultaneously, the projects aim to generate economic opportunity for the surrounding community and the corporations involved.

- Biffa has engaged in collaborative attempts to innovate on and introduce electric collection vehicles (EVCs) into their business operations. Cory Reynolds explains the progress of a recent attempt in Manchester:

> *… in our collection fleet this march (2021) we introduced 27 ECVs into Manchester as part of the contract with Manchester City Council. And that's the biggest fleet in the country. … You couldn't use ECVs in a more rural environment at the moment because the technology doesn't support that. We are working closely with JSCB and Caterpillar to move that forward and testing new technology that comes online.*

Principle 4: Measurement & Performance

As a waste management company, Biffa has a history of measuring non-financial metrics surrounding its environmental impact. As of 2020, its key non-financial metrics were tonnes of waste processed, tonnes of waste collected, lost time injury rate, CO2e emissions reduction, and employee engagement (Biffa 2020a). Of these, the implicit environmental goal of the firm's purpose is measured by tonnes of waste processed, tonnes of waste collected, and CO2e emissions reduction. Each of these KPIs have specific descriptions delineating how they are measured, and related general targets or broad strategic direction (e.g. tonnes of waste collected has the target of simply growing).

Example 2. Flood Re

The company, and principle 2: Regulation

Flood Re is a purpose-driven joint venture involving the UK government and UK insurance companies. Its purpose is to improve the availability and affordability of flood insurance (Flood Re 2020; 2016). It does this by spreading the cost of covering high risk flood insurance across the industry, which aims to help reduce the premiums required for flood insurance that otherwise would be unaffordable.

Flood Re's business model is that it collects an annual 180 million GBP levy from household insurers, who then have the option of passing the flood risk element of any insurance policies they sell off to Flood Re for a fixed rate. Surplus from the 180 million levy (profit) is added as a financial buffer that allows Flood Re to spend even less on reinsurance. Over the last four years, Flood Re has averaged a profit of approximately 115 Million GBP (Flood Re 2020), which has been used in part to reduce the reinsurance cost to the firm. As Flood Re continues to collect the annual levy and fixed rates for flood insurance packages, it will acquire an even greater financial buffer that will allow it to spend even less on reinsurance and require even less in its annual levy. The goal for Flood Re is to continue to pursue its purpose until 2039 (Flood Re 2021). After 2039, the objective is to have reduced the cost of flood insurance to the point where flood insurance can transition to a free market.

Flood Re's purpose appears to drive it to pursue a range of relatively innovative strategies that are designed to make flood insurance more affordable and accessible. Recently, the company has been involved in developing flood performance certificates, in researching ways to improve the flood resilience of homes, in modelling the impact of climate change on future flooding, and in the creation of the Flood Risk Communities' Charter (Flood Re 2020).

Principle 3: Ownership & Governance

When the company was first being created, Flood Re faced challenges developing a business model in an industry where active intervention by government to correct a market failure was not naturally welcomed and the vast majority of firms were set up to maximise profits and not social or environmental outcomes. Flood Re sought to overcome these challenges by engaging with two of its major stakeholders, the government and the insurance industry. Both parties wanted a solution and a way forward, and multiple concerns had to be actively addressed in order to arrive at a purpose-driven business model that was acceptable to both parties (Kerr 2019).

For instance, one concern was a broadly held hesitation regarding the level of intervention a government should have on a free market (Kerr 2019). Another concern was a desire by the government to avoid a contingent liability for flood risk (Kerr 2019). Additionally, industry firms were concerned about the costs they would have to incur. Brendan McCafferty, CEO of Flood Re from the firm's inception in 2014 until 2017,[3] discussed how the project's initial development required significant negotiation between himself and the two parties:

[3] Comments from Brendan McCafferty are his personal views of Flood Re while he was CEO 2014–2017.

> *They all wanted it to happen [the major insurance companies], but not at any price. And I was given a mandate to go and negotiate that legislation. That had some very close parameters. … We just managed to get it done.*

In the end, the current form of Flood Re was developed, which involves an agreed upon levy by both the government and business sector. Flood Re cooperates and relies upon regulations made by the secretary of state, and ensures the interests of the insurers are satisfied before consenting to proposed regulations (London 2014).

Since its launch, the firm appears to have continued to engage closely with insurance companies to ensure their interests are monitored and addressed while allowing the purpose to be the force that drives the business forward and shapes all activities of the business. Brendan noted this balance when he spoke about the day-to-day decision-making and activity within the firm while he was the CEO:

> *… we spend most of our energy figuring out how to make this a success for insurers. … They are our sponsors. They pay the bill. But I [also] spend a lot of time personally, making sure we are out there striking an independent voice and being very focussed on the consumer outcome. Because in the end that's what it is about. That is the purpose of the organisation.*

By continually engaging with the insurance companies and making sure the firm activity addresses their concerns, Flood Re appears to have been able to come up with ways of prioritising its purpose while addressing the interests of its funding source and core stakeholder group.

Principle 4: Measurement & Performance

To fulfil the purpose of making flood insurance more accessible and affordable, Flood Re first needed to gain an understanding of how accessible and affordable current flood insurance was. In other words, the firm needed to determine how it would directly measure performance against the purpose, rather than rely purely on metrics that indicated financial health. To do this, the firm took benchmark prices for flood insurance and availability of flood insurance for high-risk homes:

> *…we set about signing up several thousand consumers that we know to be affected by this, who are in the right parts of the world and geography. … So, we know that (the) typical customer might have zero or one insurer that's prepared to offer them any price at all. And then that price might be a premium of three and a half thousand pounds with an excess of thirty thousand pounds.*

With a benchmark in place regarding how inaccessible and unaffordable flood insurance was for at-risk homeowners, Flood Re could measure how well it improved both parameters by selectively sampling the market:

> *If you take those customers that couldn't find a price at all, could they on the 4th of April [launch date of the programme]? If they could, what was the price? How many markets could they access? What was the access like? What were the policy conditions like? And so, we had that benchmarking in place …*

According to the firm's 2020 annual report, more than 300,000 properties have benefitted from the scheme since its launch, 80% of households with previous flood claims have seen a price reduction of over 50%, and 98% of households with previous flood claims can now get quotes from at least four insurers (Flood Re 2020).

Example 3. Neighbourly

The company

Neighbourly is an SME that was one of the first B Corporations in the UK, achieving its accreditation in 2015 (B Lab 2021a). It is dedicated to the purpose of improving societal wellbeing by connecting corporations to charitable local causes.

Acting like a two-sided marketplace, corporations, who pay to use the platform, can donate volunteer hours, excess product, or funding to any of the thousands of vetted local causes on the Neighbourly platform, for whom is it free to use. Through Neighbourly, corporations are able to improve their social and environmental efforts and act more 'local,' reaching the communities near their businesses. CEO of Neighbourly, Steve Butterworth, describes Neighbourly as being, '… *a platform designed to help a corporate business activate its social purpose at a local level, but at scale, to address the perennial challenge facing corporates, which is, "How do we support all of the communities that we serve and demonstrate authentically that we are invested in the long-term wellbeing of that community?"'*

Since its inception, the firm has helped corporations donate nearly 14 million GBP, 72.5 thousand volunteer hours, and over 56 million meals (Neighbourly 2021b). Most recently, Neighbourly won the 2021 Edie Sustainability Leaders Award for its Product Surplus Program, which helps corporations donate their surplus product to cause-related organisations (Neighbourly 2021c).

Principle 1: Corporate law

Neighbourly's purpose is anchored to societal wellbeing as a whole rather than a particular strategic pathway to it (e.g., youth unemployment or helping address climate change). This broad purpose has been cemented in its articles of incorporation:

> *The purposes of the Company are to promote the success of Company for the benefit of its members as a whole and, through its business and operations, to have a material positive impact on society and the environment, taken as a whole.*[4]

The above closely aligns with the definition of purpose from the British academy in 2018 as '… to produce profitable solutions for the problems of people and planet' (British Academy 2018). While the articles of incorporation seem to position profit and purpose as two separate and equal goals (reflecting, for example, the approach taken by B Corps), the firm appears to express that its primary value generation motivation is to improve societal wellbeing through its platform with profitability serving as the means to this end, obtained through income gained by selling the service to companies.

Principle 5: Financing & Investment

Neighbourly finances its operations through corporate partners who want to improve their community relations and create positive impact. Financial resources are then used to connect corporate partners with over 17,000 verified 'good causes' that Neighbourly has personally vetted (Neighbourly 2021d; 2021e). Neighbourly identifies causes that relate to each corporate partner's goals and purpose, and actively helps them become more purpose-driven. Companies that Neighbourly have worked for with include M&S, Starbucks, Aldi, T-K-Max, Lidl, Innocent, Heineken, B&Q, Danone, Samsung, M&G, Penguin, Coca-Cola, and Southern Co-op, and Virgin Media O2 (Briggs 2020; Neighbourly 2021d; 2021f; 2021g). By connecting corporations with social and environmental causes, Neighbourly achieve its purpose of societal wellbeing.

Example 4. Interface

The company

Interface is an international carpet and flooring company focused on improving wellbeing via environmental protection and restoration. It recently articulated its purpose as 'to lead the industry to love the world'. As the company's Vice-President Erin Meezan expressed: 'By addressing some of the world's greatest sustainability challenges, manufacturers will add value for all employees, customers, shareholders

[4] See Memorandum and Articles of Association, 13 April 2021, at https://find-and-update.company-information.service.gov.uk/company/08293976/filing-history

and communities; and secure their business for the long-term' (Faversham House Ltd 2018).

The firm's move to becoming environmentally motivated was initiated by the company's founder, Ray C. Anderson. After reading a book on sustainability which exposed him to the impact that over-use of natural resources was predicted to have on society if businesses did not change their approach, he set about fundamentally reducing the firm's negative environmental impact. In 1994, as a core strategy to achieve their purpose, the firm established Mission Zero®, 'have zero negative impact on the planet by 2020' (Interface 2019).

To pursue Mission Zero®, the firm relied on the support of experts in sustainable business including scientists, activists, and entrepreneurs, to create a framework to transform the business. The resulting framework resulted in the firm focusing on seven strategic areas: 'Eliminating Waste; Benign Emissions; Renewable Energy; Closing The Loop; Resource Efficient Transportation; Sensitising Stakeholders and Redesign Commerce' (Interface 2019). The firm agreed a series of outcomes based on the framework: 'zero waste to landfill, zero fossil fuel energy use, zero process water use, zero greenhouse gas emissions' (Interface 2019). Finally, they set up three programs to achieve these goals through its seven strategies – 'Factories to Zero, Products to Zero, Suppliers to Zero' (Interface 2019). These concepts seem to have given direction to the firm in order to achieve its purpose.

In 2019, Interface announced that it had completed Mission Zero®, one year ahead of schedule; All of the firm's flooring products had achieved the status of being carbon neutral across their full lifecycle (Interface 2021a). While Mission Zero® was a goal to 'do no harm', which required a range of cutting-edge industry innovations, once achieved, the firm set its sights on going further, on producing net positive outcomes. As Jon Khoo, Head of Sustainability for Interface, commented in a recent interview with the authors:

> *We could just stop there and be like, 'We've completed sustainability by having carbon neutral products.' But that's not enough for us at interface. What if we could reduce that carbon footprint even further?*

As a result, the firm initiated Climate Take Back™, which aims at using the Interface business to create a planetary climate suitable for life on earth. Interface began researching ways to use business activity to achieve this goal. An example of such efforts is the firm's Proof Positive, the world's first carbon-negative tile, which has a negative carbon footprint at the end of its lifecycle (Jackson 2017). Proof Positive was created as a prototype and was not commercially viable in 2017, but Interface used aspects of the incorporated technology to successfully developed a carbon-negative backing for its products (Interface 2019). Interface presently has a collection of commercially viable carbon negative tiles that it sells as part of its product line (Interface 2021b; 2021c). The firm is now looking to further implement the technology from its carbon negative products throughout its product line. Khoo gives a succinct summary of the firm's innovations in carbon reduction and current ambitions:

> *We've gone from Proof Positive, which was a prototype and was not commercially viable, to actually having a commercially viable carbon negative tile, and then not stopping there but saying, 'well how can we bring the rest of our portfolio toward that?' Not carbon negative itself, but toward having even lower carbon footprint by using the same technology.*

The firm is building on its previous accomplishments and pursuing its purpose in a way that is financially viable over the longer term. In this way, Interface aligns with the notion of organisational purpose as 'finding profitable solutions for the problems of people and the planet'. Currently, 60% of the firm's carpet products come from recycled or biobased sources (Interface 2019). The Globescan Sustainability Leaders Survey has included Interface on the list of companies that have best integrated sustainability into firm activity since the survey first began in 1992. At the same time, Interface has consistently performed well financially (outside of a steep drop during the beginning of the COVID pandemic) (Nasdaq 2021).

Principle 4: Measurement & Performance

Interface has developed a number of methods for measuring its impact on the environment. For example, the firm developed a series of metrics called EcoMetrics, which were used to measure the firm's progress towards its Mission Zero goals. In addition, Interface adopted and scaled Environmental Product Declarations (EPD) across its entire global product portfolio. This allows for easier comparison of Interface with other flooring manufacturers who use EPDs. Interface also measures the number of carbon neutral certificates that are awarded to its clients, and the number of square metres of the firm's product that make it back into the firm's re-entry programmes.

In addition, Interface has used the SHINE Handprint Methodology (Norris 2015) to measure how its actions lead to positive environmental impact beyond the firm itself. For example, the firm collaborated with a supplier to provide nylon that was made from a higher proportion of recycled material. Then, the supplier sold the nylon to another producer, increasing sector-wide impact. The downstream environmental impact was measured to be a reduction of 334,000 metric tonnes of CO2e (carbon dioxide equivalent) (Interface 2019). Another example of downstream measurement using the SHINE Handprint Methodology (Norris 2015) was when the company was trying to reduce the environmental impact of its Lagrange factory. Interface collaborated with the city's engineers to develop a way to make renewable energy from the local landfill, and the landfill gas not used by Interface was sold to another manufacturer. The downstream impact of this collaboration was measured to be a reduction of 684,000 metric tonnes of CO_2e (Interface 2019).

According to Interface, measuring achievement toward the company's purpose has a number of benefits (Interface 2019). First, it helps the company to determine whether it is actually making improvements regarding is purpose. Second, it helps customers have trust in the narratives and stories that are told by interface. Finally, it gives customers the power to encourage environmental measurement and improvement of competitors by purchasing products that (1) measure impact and (2) have relatively better impact than others. This is particularly effective when the measures used between firms are comparable.

Principle 5: Financing & Investment

In order to achieve its purpose, Interface has influenced and collaborated with a significant number of external entities. The firm uses various tactics including (1) sharing 'best practices' with its value chain, competitors and other firms, (2) offering higher order volumes to suppliers that could provide recycled materials, (3) supporting and lobbying for legislation that required carpet manufacturers to create landfill diversion programmes for carpet waste, and (4) co-investing with other organisations to develop technology that helped the firm and others improve their environmental impact (Interface 2019). For example, Interface:

- Worked with Aquafil and the Zoological Society of London to develop Net-Works™, a company that works with coastal villages to make nylon out of recovered fishing nets. Net-Works™ currently collects nets in the Philippines, Cameroon and Indonesia, and has collected over 260 metric tonnes of fishing net waste from the oceans (Interface 2019).[5]
- Collaborated with city engineers of Lagrange to develop a way to make renewable energy from the local landfill (see above)
- Hosted the executives of Walmart, who wanted to learn more about how Interface had changed its business (Interface 2019).
- Worked with the Governor of California to advocate for a recycling law (Herlihy 2017)California has been the only state in the country with a law, AB2398, governing the disposal of post-consumer carpet (PCC.

[5] The 260 metric ton number provided by Jon Khoo, Head of Sustainability for Interface.

- Is collaborating with members of the global building industry such as Skanska, Gensler, and Kingspan to increase awareness of the impact of embodied carbon through an initiative called MaterialsCAN (Interface 2021d).

Principle 2: Regulation

One of Interface's most well-known purpose-driven acts was when it advocated for progressive legislation in California to further advance its landfill diversion programmes and set aggressive recycling rate goals for firms in the face of strong opposition by its peers (Herlihy 2017; Interface 2019)2019.

In 2017, California proposed legislation which helped create a progressive level playing field in recycling for the carpet industry. The proposed update to the legislation would set out specific targets for rates of recycling with challenging date deadlines for companies to conform to (Herlihy 2018). The legislative changes included the creation of an advisory board that would monitor the programme and make suggestions. At the time, the trade association Carpet and Rug Institute (CRI), which Interface was a part of and which consists of around 90% of the carpet manufacturers in the US (Herlihy 2017)California has been the only state in the country with a law, AB2398, governing the disposal of post-consumer carpet (PCC, did not support the law and was even attempting to defeat it (Interface 2019). The CEO described how the company, driven by its purpose, responded:

> *When this information came about the piece of legislation, they [CRI] said, 'We're going to hire a lobbyist and get the bill defeated because we don't want this bill.' I was disgusted. I resigned from the trade association, hired our own lobbyist, worked with Governor Brown and got the bill passed. And I am not a popular character in the flooring industry right now, but I can sleep at night* (Mainwaring 2019).

Principle 3: Ownership & Governance

One effective way to incentivise purpose is to ensure that the purpose is the responsibility/priority of senior executives of the firm. At Interface, the purpose of the organisation is supported at the Executive level by a Director of Sustainability. She has a network of employees working under her to ensure that the purpose is integrated across the firm. Helena Reid, Director of Marketing Communications for Europe, Africa, Asia, and Australia (EAAA), described how the strategy to implement the purpose is embedded within the firm, starting with the Executive and Director roles:

> *… we have a Chief Sustainability Officer sat at the same table as all the business leads making decisions. She is there to represent the fact that we need to make sure that every element of our business focusses on our core commitment [Climate Take Back™]. … She [the Chief Sustainability Officer] has a team of sustainability leads that sit in each of the regional teams. So in the Americas, in Asia Pacific, and in EMEA …*

This network of responsibility for the purpose ensures that the purpose is considered in all business decisions. Reid explains:

> *… at every point in the business decision making process … there is somebody that has that direct responsibility around our sustainability. Whether that's keeping us true to ourselves as an organisation, and true to the commitments that we've made, or looking at how we can better ourselves, and make more of ourselves.*

In the past, Interface has also used incentives to motivate employees toward purposeful goals. A program called Quality Utilising Employees' Suggestions and Teamwork (QUEST) was implemented in the early 2010's to incentivise employees to reduce waste in their job (Ryan 2013). Bonuses were connected to sustainability goals, and an annual benchmark of reducing waste by 10% each year was encouraged for each QUEST team. During its tenure, the QUEST program also cut manufacturing costs in half (Interface 2019).

Example 5. Anglian Water

The company

Anglian Water is a water supply and recycling firm in the UK. It is the largest water company in England and Wales by geography, spanning 20% of the total land area (Anglian Water 2019b). It currently supplies 4.3 million people with drinking water, collects wastewater from 6 million people, and provides leisure services to over 2 million people annually through its water parks and recreational sites. Recently, Anglian was ranked the top-performing water and water recycling company by The Water Services Regulation Authority (Ofwat) for the AMP6 time period (the 2015–2020 asset management plan period for the water industry) (Anglian Water 2019b).

Anglian Water's purpose is 'to bring environmental and social prosperity to the region we serve through our commitment to love every drop' (Anglian Water 2019a). As the purpose explicitly states, the firm is interested in both social and environmental outcomes, suggesting it has a focus on the intrinsic value of environment rather than just seeing environmental wellbeing as just a means to creating social wellbeing. It also has a particular focus on the public in the geographical region it operates in.

Anglian Water notes that it has long been focused on improving the sustainability of environment, initiated by a climate change assessment in 1993, but has now incorporated that previous work into the heart of its business via the purpose. Andrew Brown, Head of Sustainability for Anglian Water, remarks on how the purpose served to bring the previously ancillary focus on social and environmental outcomes into the core of the business:

> *What we've done over the last 10-11 years or so has been to embed sustainability into our business planning process. So, we end up with a sustainable business plan, rather than two separate things. … Our purpose is to deliver environmental and social prosperity to the region we serve through 'love every drop.' So in terms of that we've taken our approach to environmental stewardship and community investment and sustainability right through to saying actually that is a core part of our purpose.*

Principle 1: Corporate law

In 2019, Anglian Water became the first major utility company in the UK to incorporate its purpose into its articles of association (Anglian Water 2020; 2019c). Brown mentions at least three reasons for this. The first is the importance of this step for Anglian Water's authentic pursuit of its purpose:

> *There is a difference between writing a purpose statement and slapping that into your annual report and accounts, and actually embedding a purpose in your business. That's one thing we are attempting to do, and have formally done with our articles of association.*

In addition, embedding the purpose in the firm's constituting documents was seen as a method for preventing the firm from being perceived as purpose-washing:

> *… actually, it doesn't matter what we felt like we were doing and how we were acting in the public interest. Did other people in the outside world see that? Believe that? And obviously, as a company that is part of a wider industry, when some of that wider industry isn't doing as well as we might be then we can be reflected in some of their issues rather than standing on our own performance. … Unless we lock it in and demonstrate that we are genuinely willing to create this purpose, people could always think that we are just spinning a good story.*

Finally, including the purpose within the articles of association was seen as an important step for ensuring the purpose remains a primary goal of the organisation for many years to come and is governed in a way that can outlast the current members of the organisation:

> *We've got a fantastic management board who believes in this now, and we've got a fantastic set of owners who believe in this now. But that's now. What happens if we we're bought out by other investors, and they take a completely different approach? Would that be the right thing for our region and our customers? And I think that was the bit that made our people go, no, actually none of us would want that. So, it's also a signal to other investors who might be interested in us as a company, that this is what we do. This is what we believe in. You can't buy us out and change this purpose. You have to buy into this purpose.*

Principle 2: Regulation

Along with the organisation's change to incorporate purpose into its articles of association, the directors of the firm also explicitly committed themselves to considering *'the impact of the business operations on the communities and the environment'*, and *'the consequences of decisions in the long-term'*.[6]

With Board support and the purpose in the articles, Anglian Water began the process of trying to embed purpose-relevant decision-making throughout the firm. Brown talks about how the firm sought to use a collaborative approach to achieve this:

> *… one of the things we did once we embedded the purpose into the articles was then go through a refreshing process of looking at our values within the company and how we linked everybody's activities up to that purpose. So that was done through a co-creation, collaborative process with employees; To go through that and really try and understand, if our purpose is up there, how we all as individuals, no matter what your role in the company is, contribute towards that purpose.*

To further ensure achievement of the purpose, Anglian Water uses its purpose-related outcome targets as non-negotiable constraints that strategy is devised against. Brown gives an example of this process by describing the firm's previous commitment to halving its carbon footprint:[7]

> *… if we were laying a pipeline, or a water treatment works, the target of that project being to half the carbon of the previous baseline was part of the decision-making stage-gate process. A decision wouldn't just get through. It would get scrutinised. If it didn't meet that 50% target, then it was incredibly hard to unlock the funding to deliver that project. And if it genuinely, after several attempts, couldn't be made to hit that target, then that target wasn't just forgotten. That target was moved into the rest of the capital program and had to be recuperated through other gains in other places so that the entire program came in on target.*

[6] Additional commitments were made by the firm as well, but these two seem to be most directly helpful for pursuing the firm's purpose.
[7] Previous because the firm achieved this goal and now has a new goal.

Principle 3: Ownership & Governance

Anglian Water is financed by investment funds through a private limited company, and its risk structure has attracted bond holders (Anglian Water 2020). According to Brown, the current investors are encouraging of the firm's purpose, and Anglian's act of embedding the firm's purpose into its articles is an attempt to ensure future owners are similarly aligned. Anglian Water's CEO Peter Simpson, echoes Brown's earlier comment on this point and describes similar reasoning:

> *For years we've operated diligently in the background, striving to minimise our impact on the environment while positively contributing to communities. Today's change marks a new era that codifies that approach, ensuring all future owners and investors will be obligated to work in the same way, and giving regulators, stakeholders and customers the confidence that this is simply how we work.*

Upper echelon members are also incentivised to pursue the purpose. Director incentives at Anglian Water are partially based on performance in purpose-related, non-financial 'Outcome Delivery Incentives' (ODIs) (Anglian Water 2020). Often, the percentage of bonus based on ODI was around 15% of total bonus awarded. Examples of ODIs that are in-line with the firm's purposeful pursuit of environmental outcomes are leakage of water and pollution incidents. Examples of ODIs that are in-line with the pursuit of social outcomes are bathing waters ratings, affordability, fairness of bills, and drinking water quality.

Principle 5: Financing & Investment

Anglian Water was the first utility company in Europe to launch a sterling green bond, and has six currently operating (Anglian Water 2020). Further, Anglian Water has sought to make its entire capital spending programme meet the requirements of green bond investment. Green bonds and other forms of sustainable finance, whilst still under scrutiny for the scale of their impact, supposedly give companies further jurisdiction to ambitiously pursue purpose-driven objectives, and Anglian Water intends to continue to use this method of investment as it enters AMP7 (the new asset management plan period for the water industry).

Anglian Water also invests in collaborative partnerships and projects to pursue social and environmental prosperity for its larger community. Brown outlines reasoning regarding the firm's collaborative approach to waste treatment methods:

> *Traditionally, you would go for tried and tested methods, and it would be designed, built, and operated by you as the company because you've got complete control of that. When you start to think about purpose and delivering a wider social and environmental benefit, sometimes the best way of doing that is to have a more collaborative approach.*

Brown then went on to describe a particular example involving a water treatment facility in Norfolk. First, he described the status quo method:

> *… the traditional way would be to pour some concrete, build a structure, and remove that phosphate or nitrate using an energy intensive, chemical intensive process. That's great in terms of delivering the environmental value of the effluent going into that water course. But actually, it costs more money to build, to run. You're using loads of chemicals. You've used loads of concrete. You're using lots of carbon.*

As a result, the company innovated a nature-based solution to the problem:

> *A nature based solution to that is saying ok, neighbouring land owner, can we work with you to develop a natural system so this water will leave our works and work through that system, which will have the same impact of drawing the nutrients out of there, but would deliver a site that's rich in biodiversity, a site that doesn't require any energy to run, a site that doesn't require any concrete to pour, a site that delivers community value, fits into the landscape, and still delivers that environmental output that you are regulated to do.*

Developing the above natural treatment system was novel and challenged standard practice. To achieve its goal, Anglian Water worked closely with both the neighbouring landowner and the Norfolk River Trust to design, build, and maintain the facility. Anglian views this project as highly successful, and is considering the development of up to 34 similar systems in the next five years.

In another example, Anglian Water has collaborated with the British Standards Institute and the Cambridge Institute for Sustainable Leadership to develop a credible framework for exposing the core principles of a purpose-driven business (Anglian Water 2020) which will be known as PAS 808. Brown explains some of the reasoning behind the firm's efforts to encode the principles that drive genuine purpose-driven activities, and its decision to collaborate externally on developing this:

> *The other thing that we've done is we said that we want to commit to a set of responsible business principles. But, when we put the purpose into the articles of association, we didn't have that. So, we looked across the marketplace to see what is a suitable set of responsible business principles, and we couldn't find any that fit. So, we said we could create some and adhere to those, but that feels a bit like you are marking your own homework. … So, we've been working with the British Standards Institute for just over a year, discussing with them, can we create a sort of publicly accessible specification for what that would look like.*

Principle 4: Measurement & Performance

Brown believes that targets which are ambitious enough to drive innovative thinking are important:

> *You got to set a hard target to reach to stimulate different ways of making decisions. If you set an achievable target, then you tinker around the edges with things. If you set something that you don't know how to deliver, then you really go back and think about how you got to do it.*

A traditional target Anglian Water has pursued since 2010 is reducing the firm's carbon footprint in its capital delivery program. Brown outlines this target, the domain in which it is pursued, and the subsequent goal that was created after achieving the initial target:

> *In 2010, we said we are going to half the carbon footprint of the things that we build in the space of five years. And we achieved that. Between 2010 and 2015, we reduced, on average, in the capital delivery program, the associated carbon generated by about 50%. It then gets harder, so the next five years we only set a 10% reduction on top of that. To try and drive that out. But the things that we built today are 60% less carbon than they were back in 2010.*

In order to understand the broad range of risks and impacts, Anglian Water has developed measures categorised under the integrated reporting's classification of six capitals: financial, manufactured, intellectual, human, social and relationship, and natural (Value Reporting Foundation 2021).

Example 6. Natura & Co

The company

Natura and Co describe themselves as 'a purpose driven group made up of four iconic beauty companies: Avon, Natura, The Body Shop and Aesop' (Natura & Co 2020). Natura & Co was reputedly the first publicly listed B-Corp in the world (Watson 2014) and is the largest in terms of employees. The Body Shop is the largest B Corp that was founded by a woman (B Lab 2021b). Aesop is also a B-Corp, and Natura & Co plan to help Avon become a B Corp by 2026 (Natura & Co 2020).

Brand purposes

- Natura: The brand states that (since 1969) the firm's reason for being has been to create and sell products and services that promote the harmonious relationship of the individual with oneself, with others, and with nature (Natura 2021a). It therefore is focused on tackling what it sees as a fundamental problem that threatens the wellbeing of society. This purpose involves both social improvement and the improvement of the environment, so long as the improvements support either 'better' living or 'better' ways of doing business.

- Body Shop: 'We exist to fight for a fairer and more beautiful world' (Natura & Co 2021a)
- Avon: 'build a better world for women, which means a better world for all' (Natura & Co 2021b)
- Aesop: Although run on apparent environmental and social principles, Aesop does not appear to have a clear purpose that drives it, but its overarching brand proposition is 'to nourish through intelligent interactions' (Natura & Co 2021b)

Each brand has received numerous awards for social and environmental efforts (Aesop 2019; Body Shop 2020; Avon 2021; Natura 2021b). Natura & Co's overall purpose is 'To nurture beauty and relationships for a better way of living and doing business' (Natura & Co 2021c).

Principle 5: Financing & Investment

Robert Chatwin, Chief Transformation Officer of Natura & Co, describes how Natura and Co was created with the aim of being a family of organisations with complimentary purposes that collaborated to achieve the greater purpose of the group:

> *… many people will think that Natura & Co just means Natura and companies, but it doesn't. If you think about the signal of the '&', and the 'Co', it reminds you of 'eco'. We believe in an eco-system. Even more important than that is the power of the '&', and the power of the 'Co'. We believe in collaboration, cooperation, and cocreation. This is very important, because it doubles down on the approach we take … we worked to make sure that we were talking about our purpose in a way that it wouldn't become a corporate purpose, but instead would allow companies to join this family.*

In an effort to find the right members for the Natura & Co family, Robert was tasked with seeking out companies that would contribute to Natura's purpose. Therefore, purpose was one of the main criteria in acquisition selection:

> *I only had two filters when I was looking for acquisition targets, or potential partners as we call them. One was, 'Can it fit within the purpose?' And two was a channel filter, 'Would I be able to have a quality relationship with the end consumer through this channel?'*

Principle 4: Measurement & Performance

Natura Cosméticos (Natura), the founding member of Natura & Co, has a history of measuring its impact on the environment and society (B Team 2015). For example, in 2011-2013 the firm focused on palm oil, which was (1) a main component of the firm's products and (2) a central concern for its home country of Brazil, whose rainforests were being converted into land used for the production of Palm oil. Using The Economics of Ecosystems and Biodiversity (TEEB) monetisation approach (Brink *et al.* 2009), the firm compared a standard single-crop model of palm oil production to an agroforestry system they developed. Their analysis revealed that their agroforestry system would improve the environmental value of their efforts, from R$411 (US$167) per hectare in the single-crop system to R$122 (US$50) per hectare in the agroforestry system over a 25-year period (Natura & Co 2021d).

In 2014, the firm developed an Environmental Profit and Loss report (EP&L) to monetise environmental impact across the entire value chain (B Team 2015). Categories used in the analysis include Greenhouse Gas emissions, air pollution, land use, biodiversity impacts, consumption of water, pollution of water, and waste production.

In 2015, the firm began considering the incorporation of a complimentary Social Profit and Loss monetisation measuring system (SP&L) (B Team 2015), and this measurement was in use by 2018 to measure the social impact of employment on the wellbeing of Natura's beauty consultants (Behar *et al.* 2019). Also, in 2018, Natura began integrating its EP&L and its S&PL into an Integrated Profit and Loss measurement system (IP&L).

In 2020, Natura & Co (of which Natura is member) began working with B Team, the UN Global Compact, the World Business Council for Sustainable Development and the World Economic Forum to address the issues of the multitude of economic and social impact metrics around the world, and the need for a common 'language' in this area (Natura & Co 2020).

In the 2020, Natura & Co revealed Commitment to Life, which includes a series of 27 hard and soft targets surrounding social and environmental wellbeing (Natura & Co 2021d; 2021e). Examples of hard targets include (1) becoming net zero in GHG emissions, (2) sharing at least R$60 million in value with communities, (3) expanding the firm's influence on forest preservation from 1.8m to 3m ha, and from 33 to 40 communities, (4) 50% women on board/senior team by 2023, (5) working towards 30% inclusion of under-represented groups in management, (6) full traceability and/or certification for critical supply chains, (7) 20% (or more) less packaging material (in weight), and having 100% of all packaging material be reusable, recyclable, or compostable. In addition to its hard targets, the corporation has a number of soft but highly specified targets that give the firm direction as to how to achieve the purpose.

Examples of these include (1) increasing revenue streams with 55 bio-ingredients, (2) fostering collective efforts towards zero deforestation by 2025, and (3) measurable gains for consultants/representatives and sourcing communities' earnings, education, health and digital inclusion. These hard and soft targets align with the firm's focus on measuring its progress to drive purpose-driven efforts.

Natura extends its measurement of impact beyond its operations, from source to post-customer use. It asserts that only when the company cannot avoid creating emissions and negative environmental consequences in its operations, will it offset such activities (United Nations Climate Change 2021).

Principle 5: Financing & Investment

Very recently, Natura & Co raised 1 billion USD in sustainability-linked bond offers (Cision 2021). These bonds are tied to two specific goals. The first is reducing certain greenhouse gas emissions by 13%. The second is having 25% of the plastic in the packaging of products be recycled after consumer use. If these two goals are not reached by 2027, the bond offers will be subject to an increase of 65 basis points. Both of the goals of the recent sustainability-linked bond offers are in line with Natura & Co's purpose.

Example 7. Pearson

The company

Pearson is an education and publishing company, and is the third largest book publisher in the world (Statista 2020). The firm states that it is driven by its corporate purpose, 'To help everyone achieve their potential through learning' (Pearson 2021b).

Principle 4: Measurement & Performance

The firm has pursued its purpose partly through an 'efficacy agenda,' which aims to ensure the company's products are designed and then used in ways that produce genuinely positive learner outcomes (Pearson 2021a).

An important step of the firm's efficacy agenda was to design ways to measure progress against the purpose, making sure company products can bring about positive changes in learning. However, evidencing that products and services improve learning was seen as difficult to do, because developed and standardised metrics for learner outcomes seemed difficult to find. Amar Kumar, who headed the efficacy department from 2014-2017, described how a lack of measurement for educational products spurred Pearson to measure the impact of its products in relation to its purpose of helping learners learn:

> *In healthcare, for example as a pharmaceutical company, you could never sell medicine unless you knew that it worked. As a hospital you could never operate unless your outcomes were above a standard set by the health department in any country in the world. In education there's no such standard. In education anyone can develop any product. Anyone can try to sell their product with any school system, and the buyer, which is often the educator or a school system or a government' has zero way to evaluate its effectiveness. I see that, and I think Pearson now sees that as a root cause for a lot of the problems that we have. With more technology and more innovation going into education, it's only going to get worse. It's only going to get harder and harder for teachers and faculty to decide which technology to bring into their classroom, which to keep out, what is worth their money and the student's time, etcetera. So, the Purpose for us at Pearson is making sure that everything we do delivers the outcome it promises.*

As part of this agenda, internal teams at Pearson are developed to research the efficacy of their products throughout the firm's portfolio and publish their findings in efficacy reports, which are then subjected to third-party evaluation (Pearson 2021c).

A second step in pursuing the firm's purpose is setting impact goals and pursuing impact strategies in relation to learner outcomes. Amar spoke further about how the firm developed measures and targets for learning outcomes through company products and services:

> *… we said if we want to impact on scale, what does that mean? how do you define it? We defined that as helping more learners access education and be more successful with education, and make progress as a result. And then impact had scale, and the scale we defined as getting to 200 million learners annually. We want to help 200 million learners actually do well as a result of our stuff. And so you can't count the learner unless your product actually delivers what it says.*

An example of this approach to business came in the form of target measures for employee incentives in language centres. In an effort to improve learner outcomes, the firm changed employee incentives in a way that would encourage the pursuit of the firm's purpose:

> *As an example, we run a lot of language centres in China. … The people who used to be working at those centres were incentivised based on the number of people who came in. So you tried to get as many people into the centre as you could and then you wouldn't care what happened. … And, of course, no surprise we had something like a 40% or 50% dropout rate. We changed the job descriptions of those people who were responsible for bringing people in and their sales incentives to be about how many people graduated. All of a sudden, it became, 'I have to get the people who are actually going to graduate and not just anyone I can find.'*

An important element of Pearson's approach to formulating strategy to achieve the purpose is that it should help the firm grow, because this will then help it further progress its purpose. For example, while the above change in employee incentives can be seen as a clear improvement in terms of the firm's authentic pursuit of learner outcomes, Amar also believed this change, and others like it, should lead to improved performance for the firm, *'for us the key driver is making sure educators have what they need to deliver, and we see that then leading to growth.'* Of course, Pearson has struggled recently due to COVID-19 Pandemic concerns resulting in the closure of many school testing centres (Haill 2020). This makes a current analysis on the financial impact of the firm pursuing its purpose difficult.

Example 8. Quilter

The company

Quilter plc is a UK wealth management company, formally known as Old Mutual Wealth. Under their existing CEO, Paul Feeney (appointed 2012), the company states it has become a purpose-driven organisation, dedicated to the purpose of, *'create(ing) prosperity for the generations of today and tomorrow'* (Quilter 2021a). The company takes prosperity to be understood as a composite of health, wealth, and happiness based on the real needs of existing and potential customers.

For the CEO, becoming purpose-driven has *'given us a north star, it's given us a yard stick and also it's helped engage the hearts as well as the minds of our people.'* The key question he asked to drive purpose-driven business model change, was: *'What if we could create real solutions for real people, take stuff that's really only available to the highly wealthy and make it available to everybody at a price they can afford.'* According to Feeney, this purpose and business model drive the firm's strategy and operations.

Principle 3: Ownership & Governance

In 2017 Old Mutual Wealth separated from Old Mutual. As part of the separation, the Board of Old Mutual Wealth underwent significant changes to be more aligned with the new purposeful approach. The drivers and concerns of existing and potential customers were focused on in a way that had been out of scope previously, and the firm set about developing an in-house financial advice service from scratch. In effect, the company appeared to shift away from benchmark investment management in favour of solutions-based management. The firm sold off current products that were a source of profit for the firm but misaligned with the purpose, in order to develop the products that would help the firm pursue its new purpose. Specifically, the company's established life insurance businesses were sold, and funds from the sales were used to develop new product lines that would aid in the creation of personalised wealth management solutions:

> *We sold the factory and we thought about what the new business would look like. … We started thinking about how, if it's creating prosperity, we needed to have a solution-based company. So, we came up with the phase 'real solutions for real people' and this was how our company started. What if we could create real solutions for real people, take stuff that's really available only to the highly wealthy and make it available to everybody, at a price they can afford. So, we started thinking about it and then we said, "what would our products need to look like? How would they be priced? How would people access advice?*

The changes Quilter made to its business model in pursuit of its purpose, such as the creation of the Foundation and the selling of the life insurance businesses, were obviously significant changes to the organisation. In order for these changes to take place, it was necessary to bolster the membership of its Board with individuals aligned with the purpose the company had set itself. Under these changes, Quilter has not only developed a purposeful approach, but also achieved consistent improvement in its performance (Quilter 2021b).

Principle 4: Measurement & Performance

A different way of understanding and measuring success was required for Quilter's purpose-driven approach. The goal was to monitor impact relating to the difference the purpose was designed to create.

> *… we've just gone through our 900,000th customer. When this happened, we said there's 900,000 people that we're now helping with secure financial, secure retirements. Okay, then let's monitor that, are we delivering what we're saying? Are we supporting them to achieve prosperity?*

The company measures its impact on an annual basis through its shared prosperity plan. This plan is a public declaration to deliver against 10 commitments designed to ensure the company delivers for its customers, advisers, colleagues, and the communities it engages with. Key performance indicators have been identified for each commitment and these are reported in their annual report (Quilter 2020).

Example 9. Anglo American

The company

Anglo American is a large international mining company, employing over 95,000 people across 15 countries (Anglo American 2021a). The firm's currently stated purpose is: 'Re-imagining mining to improve people's lives' (Anglo American 2021b). Within the purpose statement, 'people' includes the communities in which the firm operates and the societies within which its products are used. The phrase 'improve people's lives' includes the goal of social wellbeing, and environmental wellbeing is understood by the firm as foundational to achieving social wellbeing. The focus of the purpose on 're-imagining mining' aligns with the firm's core value of innovation within the mining sector (Anglo American 2021c) and with the improvement of what has been seen as a very socially and environmentally damaging industry.

As stated previously, Anglo American and the broader mining industry have grievous social and environmental records (Philip Mattera 2013; Chepkemoi 2017; National Geographic Society 2020; Stewart 2020). Anglo has purportedly been involved in environmental damage in at least South Africa, Ireland, The United States, and Peru, has yearly issues with labour treatment (including fatalities), and has had multiple grievances brought against it by local communities where its operations exist (Philip Mattera 2013). Given the track record of the company and its relevant industry, a new firm level purpose focused on 'reimagining mining to improve people's lives' could be seen as a significant shift in focus for the firm.

Principle 5: Financing & Investment

Anglo American has made a number of financing and investment changes in recent years which appear to be aligned with its move to becoming purpose-driven. Many of these changes have been collaborative in nature.

- Collaborative Regional Developments (CRD)
  Anglo has recently sought out the advice and help of multiple entities (local and international), in order to better understand what might improve the lives of the communities in which it operates. The rationale behind the need to collaborate is outlined in the firm's 2021 annual report:

  > *For our mines to be safe, responsible and productive, they should operate in areas that are thriving. In many places, addressing the challenges to achieve this is too large and complex to be solved by one institution alone, and instead is better tackled through collaboration and partnership.*

In line with this reasoning, Anglo American has developed an approach called Collaborative Regional Development (CRD). CRD involves Anglo American seeking to act as a 'catalyst for change' in regions where it has operations, collaborating with the community and other organisations to build social and economic value for the community beyond the firm's normal influence. So far, the CRD approach has been implemented in South Africa, Botswana, Brazil, Colombia, Peru and the UK.

- Deforestation and Reforestation

  A major issue related to Anglo American's purpose is deforestation as a result of its operations. The firm states that it has taken both independent and collaborative measures to address the issue.

  An interesting and controversial example relevant to this topic is the firm's environmental efforts in its mining operation in the Minos Rio area. Anglo has acquired over 15,000 acres of offset sites (protected environmental areas to offset the damage done to other areas). 12,000 of this the firm manages directly. The rest is intended to be donated to the Minas Gerais State government. Since first acquiring the land, Anglo has invested 3.5 million dollars in the conservation of the 12,000 hectares that they manage, and another 6.4 million into the restoration of a separate 1,300 hectares in the area. A further 2.4 million was invested for monitoring the fauna in the areas, and 2.8 million was donated to reforestation of native trees in previously damaged areas (Anglo American 2021a).

  The Minas Rio area is one of a number of collaborations and investments that Anglo American is making with the stated goal of improving the biodiversity of the regions it operates in (Anglo American 2021a). The firm has partnered with NGOs to restore other wetlands. Additionally, the firm has developed partnerships with universities to develop new insights into conservation and restoration.
- Other Recent Examples of Collaboration Activities:

  In 2020, Anglo American announced its collaboration with Accenture, Ecolab, Schneider Electric, the World Economic Forum, and Uplink, to support The Circulars Accelerator (Anglo American 2021a; Circulars 2021). This accelerator is directly in line with Anglo American's innovation-centric purpose, as the project is designed to spur innovation toward the circular economy.

  In 2020, Anglo American signed the Sea Cargo Charter, along with some of the world's largest energy, agriculture, mining and community companies (Anglo American 2021a; Sea Cargo Charter 2021). The charter established a standardised framework for reporting on and measuring emissions.

Principle 3: Ownership & Governance

One of the firm's major vehicles through which it lives its purpose is the FutureSmart Mining™ Programme, which uses a focus on innovation and technology to help the firm achieve ambitious social and environmental objectives (Anglo American 2021a). The FutureSmart Mining™ Programme, within which sits the firm's sustainability plan, feeds into three main components of the firm's employee incentive structure: Safety, Health and Environmental (SHE). These three components of employee incentives exist in different forms and amounts from the executive director level and below. Where applied, SHE goals make up approximately 20% of the incentive structure. The firm's annual report exposes the incentive structure, giving exact percentage weights for each objective for each director (Anglo American 2021a). Most director incentives structures conform to the 20% SHE objectives benchmark.

Principle 4: Measurement & Performance

Anglo American places its firm measurements into 7 value categories: safety and health, environment, socio-political, people, production, cost, and financial (Anglo American 2021a). 17 subcategories of KPIs underpin these seven value categories, and all of the social/environmental subcategories are connected to target objectives relating to various aspects of the firm's purpose or strategy to achieve it. Some of these measures and objectives are proactive in that they seek to make positive contributions (e.g., net positive impact on biodiversity), while others are focused on minimising negative effects (e.g., zero worker fatalities). At least one target (2020 Greenhouse Gas emissions targets) has been achieved a year ahead of schedule and the firm has set a new goal to both achieve carbon neutrality across all of its operations by 2040, and to have eight of the firm's operations carbon neutral by 2030 (Anglo American 2021a).

Example 10. BT

The company

BT Group plc (hereafter referred to as BT) is an international telecommunications group, operating in 180 countries (BT 2021b). The firm has numerous business lines ranging from sports broadcasting to digital security to communication networks, but the company is known as the UK's largest provider of fixed-line voice and broadband and the UKs largest mobile network operator.

BT started its recent journey to become purpose-driven under Gavin Patterson who was CEO between 2013-2019. It was during this time that the role of 'Head of Purpose' was created to advance this journey. BT's current purpose is 'we connect for good' (BT 2021b). This purpose is a change from its previous articulation of its purpose in its 2020 annual report, 'To use the power of communication to make a better world' (BT 2020). The newest articulation of the firm's purpose seems to be part of company efforts to broaden the scope of the firm and the BT brand (Dawood 2019), with broader terms such as 'connecting' and 'good' replacing the more narrow descriptors 'communication' and 'better world.' Despite the change, the firm's specialty in communication remains at the heart of many of its activities, and the concept of 'good' continues to be about bettering the world for others, as expressed by now CEO Philip Jansen in the 2020 annual report of the organisation:

> *We are here to connect for good – for the good of our customers, the good of our colleagues, and the good of our country.*

The interpretation of their purpose as using connections to solve problems of people and planet is described in the firm's 2021 annual report (BT 2021a):

> *Our purpose is as simple as it is ambitious: we connect for good. There are no limits to what people can do when they connect. And as technology changes our world, connections are becoming even more important to everyday life. We champion these connections and empower people and organisations to get more from this emerging world, removing limits and unlocking potential. We harness the power of technology to help solve some of the world's biggest challenges such as cyber security, the global pandemic and climate change.*

Principle 3: Ownership & Governance

The first responsibility stated in BT's Board responsibilities in the 2021 annual report is to establish the group's newly articulated purpose (BT 2021a). Additionally, the board has established six committees that help it pursue the firm's strategic objectives, and one such committee, the Digital Impact & Sustainability Committee, is directly charged with ensuring the purpose is progressed. Moreover, in 2020 the firm established a Colleague Board, which consists of 10 members representing the firm's business units. Members of the Colleague Board are decided by evaluation of individual employee applications, by the Colleague Board Nominations Committee (BT 2021c). Each member holds his or her position for a tenure of two years. The Colleague board is currently chaired by Isabel Hudson, a non-executive director for workforce engagement (BT 2021a). The Colleague Board's role is to provide feedback on BT's Board of Directors activity as it goes out to the rest of the company, and also to provide input regarding possible future directions for the firm. In 2021, the Colleague Board gave advice to the chief executive specifically in regard to the company's newly articulated purpose, and was involved in subsequent communications to the company's employees.

The same committee set up to integrate the firm's current purpose was also responsible for integrating its previous purpose (BT 2020). Part of the integration process involved the establishment of a specific team to implement the purpose throughout the organisation's activities. Richard Spencer, former director at BT and member of the firm's Purpose of Business Team, discussed how a group was created in the organisation to help the firm embed the purpose in its culture and pursue its purpose in its operations. First it started with a general move to consolidate CSR and Sustainability efforts to have a more unified impact on society:

> *It was historically two teams, our corporate responsibility team and our environmental sustainability team. … when we combined them, we decided to call the sort of activity we were doing a program. We called it the better future program. For a while that served us quite well to have a more structured conversation with the whole company and externally as well with ways in which we could make a difference in society.*

Then, the company developed its purpose statement and relaunched the team as a change agent in the organisation for pursuing the purpose:

> *We're not going to have a program anymore as such, but we have the purpose for business team and we see ourselves now much more as transformation agents working across the company…*

The Purpose for Business Team was tasked with integrating the purpose throughout the organisation, and helping everyone in the company connect their work to the purpose of the organisation:

> *What we really want to try and do is get people to connect with their day jobs and see that there's a why and an outcome beyond revenue and profit. It actually says there's an outcome in society that actually matters to me that our products and services are delivering.*

Finally, non-financial incentives were introduced into the board's annual bonus scheme in 2020-2021 in a way that is broadly aligned with the purpose (BT 2021a). Specifically, 5% of the annual bonus is determined by the firm's digital impact (positive social impact related to digital), and another 5% is determined by the firm's sustainability performance.

Principle 4: Measurement & Performance

In 2016/17 BT devised a strategy that was directly in line with its purpose at the time (BT 2017a). The strategic goals fell under three categories: connecting society, supporting our communities, and pursuing environmental benefits. Underneath each were specific metrics (e.g., give 9 out of 10 people access to high-speed broadband). At least one of these goals, reducing carbon emissions in the company by 80%, was achieved ahead of schedule and the firm established a new objective of 87% reduction by 2030 (BT 2017b).

In 2021, BT's new evolution of its purpose is also accompanied by social and environmental objectives, including (1) helping 10 million people improve their digital skills, and (2) an already existing goal of achieving net zero emissions by 2045. BT achieved its goal of helping 10 million people improve their digital skills during 2021, five years ahead of schedule. After achieving this target, the company created a new target, 25 million people by 2026 (Jones 2021).

Concluding analysis

While the primary goal of this article is to provide descriptive illustrations, a number of important analytical points arose during the developing, writing, and reviewing of the included cases. We include the most relevant points in this section.

Current progress towards the principles as common practice

Taken as a whole, the illustrations provided in this article cover practices that are associated with all eight *Principles of Purposeful Business* (see Tables 1 and 2). At least one illustration was readily found for each practice area, and for many practices multiple illustrations were found. However, no illustration readily covered all principles, although that is not to say that more investigation would not have uncovered more examples within the organisations. This can therefore be seen as an indication that, while genuine attempts to transition to being purpose-driven are occurring, the journey to purposeful business is still in a nascent period. This article marks just one initial contribution to documenting some of the journey for some organisations.

Ownership and governance

A well-known question regarding purpose is how companies react when a purposeful approach leads to less than ideal financial returns (Cruz 2021; Deans 2018). The broader question is how purposeful companies address pushback and resistance from those who have a financial or ownership stake in the organisation. Of the eight principles from the British Academy, this question and its associated context falls most easily under ownership and governance, and only two illustrations (Quilter and Flood Re) expose a situation where resistance was met. Outside of these examples, the illustrative evidence for governance and ownership seems to focus on managerial incentives. This focus, and the lack of discussion about difficult situations and moments of trade-off between purpose and other company priorities, may suggest the participants focused on the confirmatory (i.e., they focus on the times when purpose works). It was beyond the scope of this article to investigate what happens when purposeful businesses face the aforementioned sources of resistance and are forced to change tack. However, this would be a fruitful subject of future research, including identification of the barriers to purposeful business, as well as successful methods to avoiding or overcoming such barriers.

The need to better understand and verify success towards purposeful outcomes

Purposeful businesses focus on solving problems for people and planet and not profiting from harming either (British Academy 2018), and a full evaluation of purposeful practices would include verification of whether or not true problems have been truly solved. This topic (determining how to truly impact wellbeing outcomes and verifying whether company efforts are truly improving wellbeing outcomes) seems to be one of the more challenging aspects of the purposeful business approach but one which is garnering greater attention.

Consider, for example, the Anglo American activity of creating 'offset sites' for reducing environmental impact. Offset sites are controversial because the positive protection of an area is 'offsetting' simultaneous negative impacts on another area (Virah-Sawmy 2014). Anglo's direct mining work in Minos Rio (not an offset site) has been the subject of negative criticism by the London Mining Network, with numerous allegations of environmental and social violations (London Mining Network 2017). Thus, while offset investment is indeed in line with the company's purpose, the effectiveness of the company's pursuit of its purpose is contestable.

Interface, on the other hand, used the SHINE Handprint Methodology (Norris 2015) to attempt to develop a robust understanding of the ultimate environmental impact of firm efforts. This methodology identified not only direct impact, but also downstream impact of firm activity on the environment. Even here, the company focused on particular business activities rather than company activity as a whole.

Another complication to validating the pursuit of purposeful outcomes is that the measurement of achieving wellbeing can be complex and cannibalise core business models. For example, consider Biffa's measurement approach to its purpose. One of Biffa's goals is to reduce the amount of waste its customer's create, while another of Biffa's goals is to achieve growth in its KPI of processing waste (Biffa 2020a). This makes sense from a business model continuity sense if there is currently room for an increase in the percentage capture of customer waste or if plans to adjust to a more sustainable business model are underway.

The complexities mentioned above are not isolated, but rather provide examples of a core challenge that many, especially incumbent, purpose-driven businesses face and which this article helps illuminate. In short, is it difficult to systemically address society's social and environmental problems through business when business models, systems, and structures are often co-dependant with the many of society's social and environmental problems. The illustrative examples presented in this article give a partial window on these complexities as well as a sense of the momentum for change.

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To cite the article: Ebert, C. & Hurth, V. (2022), 'Principles of purposeful business: illustrative examples', *Journal of the British Academy*, 10(s5): 163–207.
https://doi.org/10.5871/jba/010s5.163

Journal of the British Academy (ISSN 2052–7217) is published by
The British Academy, 10–11 Carlton House Terrace, London, SW1Y 5AH
www.thebritishacademy.ac.uk