

# HABERMAS ON THE HIGH STREET

CAN LAW ENCOURAGE SUSTAINABLE THINKING IN BUSINESS?

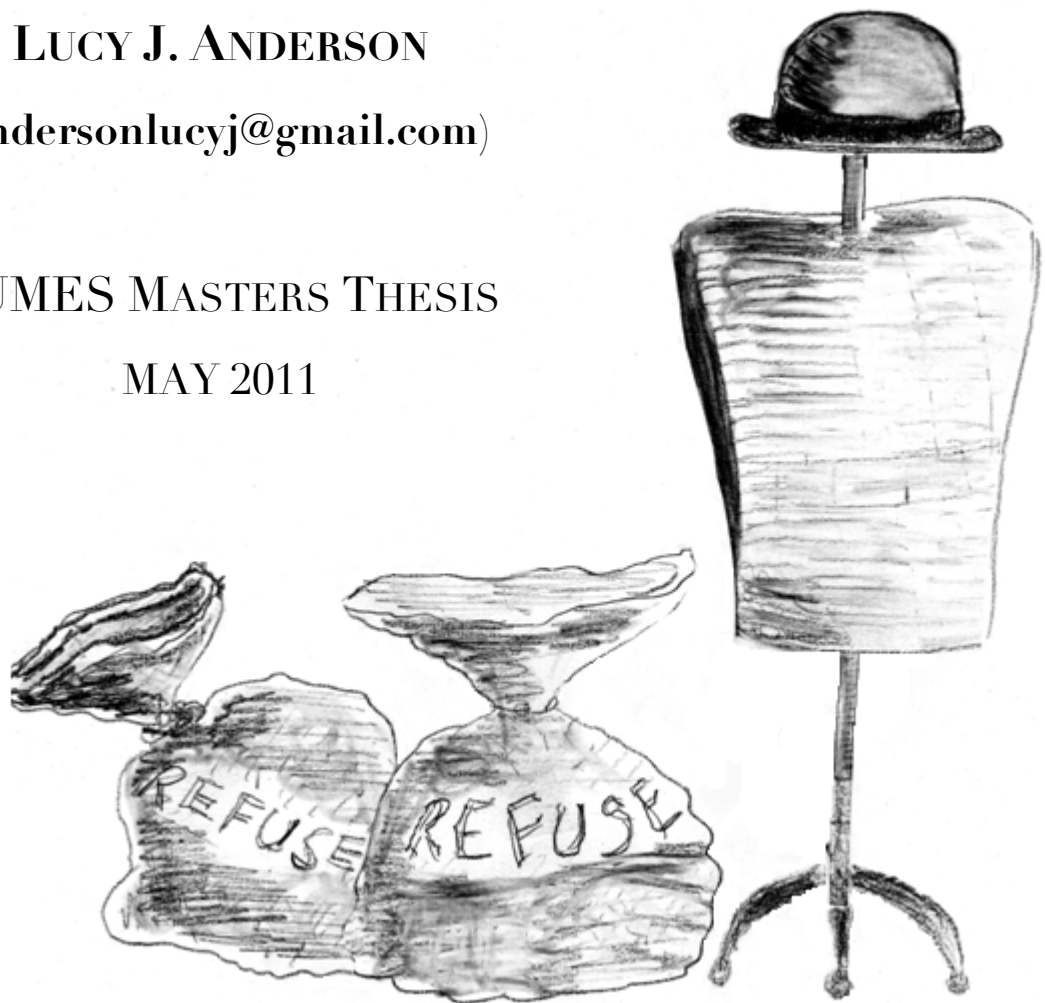
A STUDY OF UK FASHION RETAILERS

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LUMES MASTERS THESIS

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## ABSTRACT:

On the understanding that our consumer society has profound effects on our environment and that business plays an intrinsic role in solving this problem, in this thesis I examine whether law can promote long-term and multi-stakeholder considerations in the business decisions of company directors. Focusing on an empirical study of the British fashion retail industry and from a sociology of law standpoint, I evaluate s172(1) of the UK Companies Act 2006. This provision outlines those matters that directors must *'have regard to'* when considering the actions which are *'most likely to promote the success of the company'*. I find that the provision is limited by ambiguity of purpose and requirements, and lacks enforcement mechanisms. I make recommendations of amendments to the Provision which could enhance sustainable thinking in the business community. Using Habermas' theory of law I consider the consequences of these suggestions for the legitimacy of the law, and the potential influence it could have on reducing the negative environmental effects of our consumer society. I find that my proposed changes would undermine the legitimacy of the law and consequently reduce levels of compliance. In conclusion I reason that s172(1) has little effect on directors' decision-making and that the embedding of comprehensive environmental management at the boardroom level requires a more complete review of existing corporate law.

Key words: Consumption, Corporate Governance, CSR, Directors, Fashion, Habermas, Law, Sustainability

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### ABBREVIATIONS

**CECP** – COMMITTEE ENCOURAGING CORPORATE PHILANTHROPY

**CSR** – Corporate Social Responsibility

**DEFRA** – Department for Environment, Food and Rural Affairs

**DTI** – Department of Trade and Industry

**ESV** – Enlightened Shareholder Value

**FFTF** – Forum For the Future

**LCA** – Life Cycle Analysis

**M&S** – Marks and Spencers

**PLC** – Public Limited Company

**The Act** – The Companies Act (UK) 2006

**The Provision** – s172 of the Companies Act (UK) 2006

**UKFR** – UK Fashion Retailers

Clothes make the man.

Naked people have little or no influence on society.

(att. Mark Twain)

## Chapter 1: CSR, CORPORATE GOVERNANCE AND SUSTAINABLE CONSUMPTION

Western society is characterised by a profound obsession with material consumption. This way of life has contributed to better health, longer lives and economic prosperity. However, our addiction to ‘stuff’ has serious consequences for our planet (Goleman, 2009). Scientists now believe that we have reached ecological limits in a number of areas that are fundamental to continued life on Earth (Rockstrom et al, 2009). It has become apparent that if we are to preserve sufficient resources, retain eco-system services and prevent the effects of disastrous climate change for future generations, then we must seriously consider our current lifestyles.

On the other hand it is also recognised that there is a disparity between the lifestyles of some: which have produced dramatic ecological consequences and that of others: which have had a much smaller effect on our planet. The internationally recognised ‘Polluter Pays Principle’ states that those who benefit from environmental degradation should also be responsible for the negative ecological consequences of their gains (Hughes et al. 2002). In part this principle led to the now widely accepted notion that businesses are responsible for the environmental (and social) consequences of their acts in pursuit of profit (Epstein, 2008).

In response to this, governments have introduced considerable environmental regulation to ‘command and control’ the activities of the business world (Richardson and Wood, 2006). This legislation has banned toxic chemicals, protected wildlife and curbed energy use (Hughes et al. 2002). Whilst environmental law has helped protect our environment to a certain extent, it is also apparent that more has to be done. Critics complain that environmental regulation is reactive, ‘cumbersome’ and ‘costly’ (Bosselmann, 2006:4). There are also problems with compliance (McBarnet, 2007). Most recently commentators have begun to notice that it largely ignores ‘end of pipe’ issues and demands of consumption: surely a driver in the production process (BSR, 2010).

Encouraged by both regulatory and societal pressures businesses are making some headway in reducing their impacts during the production process, but little has been done to address the role of companies in relation to consumption (Hobson, 2004). Despite the realisation that corporate responsibility is ‘*ineffective*’ without ‘*concerned consumption*’



(McBarnet, 2007:17); most governments (and certainly that of the UK) see *'sustainable consumption as [a] primarily individualistic economic issue'* (Hobson 2004:133). This, some have argued, fails to appreciate the systemic aspect of sustainable development, which calls into account the actions of a multitude of stakeholders (ibid). Certainly it does not address the role played by business in encouraging consumption (BSR 2010); with concern for short term economic success, companies are eager for consumers to buy more (Jackson & Shaw, 2008). Addressing this goal might go some way to re-evaluating the promotion of sustainable consumption.

Short-termism is an endemic part of most business entities (Worthington and Britton 2006:452, BSR 2010:8) which often undermines any sustainability goals (Gunningham et al. 2003:45). It has been convincingly argued that the lack of foresight and immediate maximisation of shareholder value is a consequence of current codes of corporate governance (Mitchell 2007:301).

Consequently calls have been made for greater integration, which put sustainability issues at the heart of corporate matters (Richardson & Wood 2006, Epstein 2008; Mitchell 2007). As the proponents of company strategy, many have emphasised the key role management can play in the promotion of sustainable business goals (Gunningham et al. 2003; Guerra et al. 2009; Epstein 2008). Consequently it makes sense to consider how corporate governance can encourage long-term reflection on environmental issues by business executives.

There are a number of ways in which the profile of sustainability issues and environmental concerns can be raised within the boardroom. Some recommend NGO and community activism (Gunningham et al 2003:31) whilst others look to increased involvement of junior members of staff (Centre for Sustainable Fashion: 2009) and some advocate programmes of cooperation and voluntary reform (Caby & Chousa, 2006). It has been contended that these 'soft' approaches fail to take into account the strength of the financial constraints imposed by the market (Wood, 2006 and Epstein 2008). Jürgen Habermas, considers that legislation can counteract the effects of the market on human decision-making and, as a growing number of countries address sustainability through legislative amendments to current corporate governance structures, it would appear, he is not alone in his thinking (Gunningham et al, 2003; Lozano et al. 2008).

## 1.1 THESIS OUTLINE

### 1.1.1 RESEARCH QUESTION AND AIMS

In this thesis I have reviewed the approach of the UK Government, who, in 2006, enacted s172 of the Companies Act (“the Provision” and “the Act”) which attempts to promote sustainable thinking in company directors. I used Habermas’ theory of law and a case study of the UK fashion retailing industry to answer my research question:

**Can s172 of the UK Companies Act 2006 promote sustainable thinking in the business decisions of company directors?**

Numerous commentators have highlighted the need for more research, not only on corporate governance, environmental management (Cordeiro & Sarkis, 2008) and board process (Guerra et al, 2009) but also in relation to socio-legal aspect of environmental law (Richardson and Woods 2006). I have attempted to address some of these issues and the concerns that both fashion and corporate governance research is dominated by quantitative and positivist studies (Hodge et al. 2007; Scherer and Palazzo, 2007).

I chose a qualitative method of analysis in an effort to develop a deeper understanding of the issue (Yurchisin & Johnson, 2010:21). I fully appreciate the criticisms of bias that surround such research (Bryman, 2008) but hope that by using the theoretical approach of a recognised social theorist, my research will have some wider applicability. My own epistemological view supports those who believe knowledge and perception is socially constructed and I think Habermas would agree that universal truths cannot be gleaned from a single perspective. Nevertheless I sought to limit the potential bias both in my choice of industry and in my research methods. These processes will be discussed in more depth later.

### 1.1.2 STRUCTURE

Before I answer my research questions I must begin by further elaborating on, not only the key issues that I wish to address, but also the standpoint from which I will consider them. Consequently in the first part of this thesis (“Business, The Environment and Law”) I outline my perceptions of the current issues surrounding sustainable consumption, business practice and the role of corporate governance. I then discuss socio-legal theory (particularly that of Jürgen Habermas) and why I found it a useful tool of analysis for my research question (“Law and Critical Theory”).

I used a combination of legal research and empirical study, and the methods I employed and justifications for my decisions are outlined in the ‘Methodology’ chapter. In my findings chapter (‘The Limits of s172’) I review the key criticisms of the Provision and evaluate the effects, using examples from the UK fashion retail (UKFR) industry.

Then, using UKFR as my point of reference, I make suggestions as to how s172 might be made more effective in promoting sustainable thinking in business (‘Integrating Sustainable Thinking into s172’). I take these amendments and evaluate them from a Habermasian perspective (‘Legitimacy and The Law’). Finally in my discussion section (‘Moving on from s172’) I try to draw together the ideas to produce coherent and applicable answers to my research question and I make suggestions for future research.

## 1.2 DEFINITIONS OF KEY TERMS

Part of the process of explanation and applicability of my research requires clarification of the terms and concepts I use in my study and analysis.

### 1.2.1 SUSTAINABILITY, SUSTAINABLE DEVELOPMENT & SUSTAINABLE THINKING

**Sustainability** is notoriously ambiguous and many interpretations of the term exist (Dresner, 2002). My view is that sustainability is the goal of balance between anthropological and ecological systems: a human society that works within environmental boundaries. It is not the same as sustainable development.

**Sustainable development** famously categorised by Bruntland as *‘meeting the needs of the present without compromising the ability of future generations to meet their own needs’* (Bruntland: 1987) is the means by which we reach the goal of sustainability (Richardson and Wood, 2006). It takes an anthropocentric stance and encourages the balance of economic, social and environmental systems. Some would argue that this approach fails to fully accept the importance of ecological boundaries on our social system (Bosselmann, 2006) and thus would suggest that my definition falls within the confines of ‘weak sustainability’ (Dresner, 2002). However, I intended to focus my research on environmental management and, to the extent that prioritisation of ecological concerns inevitably leads to a re-evaluation of the importance of economic growth<sup>1</sup>, this thesis embraces a form of capitalism not unlike that proposed in the steady-state economics (Daly: 2008).

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<sup>1</sup> Although some might disagree with this statement (Porter & van de Linde, 1995)

There is no clear definition of sustainable development in UK legislation (Ross, 2010) but recent reports suggest that it falls within the ecological modernisation paradigm (DEFRA, 2011a) With its advocacy of the necessity of economic growth, this is a paradigm within which most businesses comfortably fall. Therefore, whilst my definition of sustainable development is not one that could be deemed eco-centric sustainability it does offer a pragmatic bridge between these two schools of thought.

I think that the factors outlined in s172 (see **Box 1**:p32) offer a broad example of the necessary considerations for sustainable development and for ease of discussion, in this thesis I refer to these factors as **sustainable thinking**.

### 1.2.2 CSR V CORPORATE GOVERNANCE

A 2001 EU Green paper on **CSR** describes the idea as “*a concept whereby companies decide voluntarily to contribute to a better society and a cleaner environment*” (as quoted in Bergkamp 2002:138). By voluntary we can presume they mean not legally required: for CSR campaigns are rarely motivated by morals alone (Worthington & Britton, 2003). Shareholders, competitors, media and citizens all encourage companies to act more sustainably (Gunningham et al, 2003). However, CSR is now widely recognised to encompass both voluntary and de jure acts. I will discuss this in more depth in chapter 2. In my research I adopted the attitude of Doreen McBarnett that : “*CSR is not philanthropy: contributing gifts from profits, but involves the exercise of social responsibility in how profits are made*’ (2007:9).

**Corporate Governance** some would argue is an essential part of any CSR strategy (Mitchell, 2007). The terms, however, are not intrinsically linked. A somewhat ‘*slippery expression*’ (Loughrey et al. 2008:79) corporate governance is essentially the ideas behind and the rules dictating the structure of a commercial organisation. The 1999 OECD principles of corporate governance define ‘*good corporate governance [as being] concerned with rules and practices that govern the relationship between managers and shareholder of corporations as well as shareholders like employees and creditors*”(Ho. 2010:18). It may, therefore, have very little to do with CSR and be designed entirely for profit maximisation.

### 1.2.3 DIRECTORS

The definition of director is also a confusing term. Debate has arisen over whether managers, non-executive directors and directors bear the same responsibility under law (Mortimer 2009; Davis, 2008). Such discussion is outwith the scope of this thesis and, for the most part, I have used the word's management, executive and director interchangeably, to mean those involved in company decisions at the boardroom level.

### 2.1 THE ROLE OF LEGISLATION IN CSR

The debate surrounding corporate responsibility and business endeavours has been raging since the 1970's and Milton Friedman's now infamous observation that *'The Social Responsibility of Business is to Increase its Profits'* (Friedman, 1970). There are people who still advocate Friedman's belief that voluntary CSR and corporate philanthropy is undemocratic and unaccountable (Wood, 2006) and that *'socially responsible business is best imposed through regulation'* (Gunningham et al, 2003:1).

However, in today's business world the majority of people support the idea that corporations must take heed of the social and environmental consequences of their actions (Epstein 2008:19) and evidence would suggest that there are few who explicitly justify environmental and social harms in the name of profit (Gunningham et al, 2003:21). The popularity of this norm has led many to suggest that businesses are well aware of their responsibility and can best manage their own sustainability policies, with these strategies often reaching beyond the ambit of traditional legislation (Caby and Chousa, 2006).

Many have recognised the limits of the 'command and control' style of environmental regulation regarding it as reactive, rigid and blighted by non-compliance (McBarnet, 2007). Voluntary codes, some argue, can be tailored to a specific company's needs: they can react more quickly to public pressure for change and they can enjoy higher compliance rates (Wood 2006). Conversely the compliance and monitoring of environmental regulation is so lax that, in some areas, it could be argued that adherence to legislatively imposed limits is effectively voluntary.

In truth the distinction between voluntary and de jure CSR is rather fuzzy. Companies have been held legally accountable to their voluntary codes of practice: in the 1990s Nike was sued for failing to adhere to its own labour standards (McBarnet, 2007). In recent years the idea of business leading the way in sustainable practices has been widely promulgated and many support the idea that CSR should be a combination of both regulation and voluntary business initiatives. Whilst the 'green-gold' scenario advocated by Porter (1995) has come under criticisms for its utopian outlook (Gunningham et al.

2003: 145) it seems sensible that any business which wants continued long-term success must take into account the opinions of a variety of stakeholders. Gunningham et al. argue that a successful business is given a *'licence to operate'* by society. That licence comes from 'legal stakeholders', 'social stakeholders' and 'economic stakeholders' (ibid: 35). In this 'stakeholder theory' a successful business must take into account the views and limits set by regulation, the local community and the market (Crane & Matten, 2007).

Up to a point companies are beginning to adopt a more responsible approach to their business management. A combination of regulation, market incentives and community action is slowly making production more sustainable. Waste reduction, energy conservation and promotion of the triple bottom line is ensuring that supply chains are moving towards more ethical and environmentally friendly productions. Numerous companies now use life-cycle analysis (LCA) to establish where changes can be made (Goleman, 2009).

Nevertheless, despite major moves towards more sustainable production, many believe that CSR is limited by financial constraints (Worthington & Briton, 2006; Hess, 2006). This idea is strongly supported when we consider that the area most likely to hit the economic bottom line – the issue of consumption – has largely been ignored by the corporate world (BSR, 2010).

## **2.2 BUSINESS AND CONSUMPTION**

The link between corporate responsibility and consumption is complex. Recently retailers and producers have been called upon to provide consumers with more information regarding the origins and manufacture of their products. This may allow consumers to dictate through purchase power how they wish companies to operate (Goleman, 2009) and falls within the traditional view that consumption is an individual responsibility (Hobson, 2004). This simplistic interpretation fails to address the complexity of information facing today's consumer in their purchase choice (Lebel 2005:11).

Similarly it underestimates the power of businesses (particularly large corporations) to encourage us to buy more (ibid). Consumption is based on a variety of drivers from price to look to lifestyle (Røpke, 1999). Consumers may want more environmentally friendly goods – and rising levels of consumption of ethical products and services would suggest this (Cooperative Bank, 2010) – however, consumption is also highly irrational and faced

with a variety of information and in the heat-of-the-moment of impulse buys, consumers may not actively consider the environmental consequences of their actions (Lebel, 2005; Goleman, 2009). This has been termed the 30:3 paradox: where 30% of people claim to be concerned about the ecological effects of their products, but yet reflect this concern in only 3% of their purchases (Sustainable Consumption Roundtable, 2006).

It has been recognised that corporations play a key role in inciting our irrational purchase choices. Naomi Klein's best-seller 'No Logo' (2000) argues that business no longer sells just products but also ideal lifestyles, images of which cloud our judgment when we shop. This is now a widely accepted notion and marketing-savvy consumers are becoming increasingly wary of business intentions. Paradoxically this may be reducing positivist responses to CSR strategies as consumers dubiously regard ecological business as 'greenwash' (Futerra, 2008; Goleman, 2009).

The extent to which business is responsible for our levels of consumption is, of course, debatable. However, there does appear to be a growing realisation that consumers cannot address the issue of consumption alone and that businesses must also play a role in reducing and greening our consumption patterns (Sustainable Consumption Roundtable, 2006). Obviously this poses a dilemma; how can businesses- whose primary purpose is to make profit by selling products – actively help reduce consumption?

One argument that has been made is that businesses must begin to adopt a more long-term pluralistic strategy to sustainability (Richardson & Wood, 2006). This can be achieved through incorporating sustainability ideas in product design (Deutz et al, 2010) or by engaging with, rather than '*managing*', customer expectations (Gunningham et al, 2003); numerous solutions have been suggested. What does appear to be universal is the idea that sustainable thinking must become an integral part of the business (Hess, 2006). This leads to the consideration of corporate governance as an avenue to promote sustainable development.

### **2.3 SUSTAINABLE THINKING AND CORPORATE GOVERNANCE**

If the goals of sustainability are to be fully embraced by business, ensuring their promotion within corporate governance is essential (Mitchell, 2007) Some argue that a good corporate governance structure can have similar outcomes to a comprehensive CSR strategy (ibid). There are a plethora of actors and relationships involved in corporate governance, however the individual who receives most attention in the literature is that of



the company director. It has been said that *'the board of directors is the core of the corporate governance systems'* (Guerra et al 2009:198).

The scandalous collapse of Enron and the recent banking crisis has led to an increasing distrust of directors (Hess, 2006; Epstein 2008). A wave of popular documentaries - including *The Corporation* (Achbar & Abbot, 2003) and *Inside Job* (Ferguson, 2010)- have done little to quell this bad-guy image. Certainly it has been shown that poor directors rarely lead a successful company: as Bob Garratt's book on company directors puts it *'The Fish Rots From the Head'* (2010).

Conversely good management can have a profound effect on a company's success particularly in relation to environmental concerns (Epstein, 2008; Gunningham et al. 2003). Many believe that encouraging sustainable management is key to sustainable business (ibid; Mitchell, 2007) and most executives concur that *'sustainability'* is *'very or extremely important'* in business (McKinsey & Co: 2010).

Then again many companies still fail to whole-heartedly embrace sustainability in their business strategy (Epstein, 2008), particularly in consumer facing industries<sup>2</sup>. Some argue that this failure is a result of the *'legal nature of the corporation which tends to remove responsibility from those making decisions'* (Korten, 1996:49) whilst others acknowledge that executives are constrained by the necessity to realise short-term economic goals for the company (Gunningham et al, 2003).

In the UK the debate on how best to encourage director responsibility and to promote sustainable thinking in business has been running for the past few decades. A wealth of voluntary codes and reviews were adopted and undertaken (Smerdon, 2007). In 2006 the Government decided to enact legislation to promote responsible decision-making in business and so the controversial s172 of the Companies Act was born (Mortimer, 2009).

This follows the understanding that law is an intrinsic component of corporate governance and whether one falls within the Friedman *'de jure'* camp or supports a more *'de facto'* approach, most commentators agree that law helps set the facilitative, regulatory

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<sup>2</sup> A 2010 report on *'How Companies Manage Sustainability'* found that executives in business to business companies were more likely (20%) than consumer based companies (14%) to see sustainability as an opportunity (McKinsey & Co. 2010).

and constitutive organisational environment (Edelman & Suchman, 1997:483). That, however, does not mean that all laws are equally useful in promoting environmental management in business (Gunningham, 2007) and so we must also critically evaluate the law.

Before presenting my findings and analysis on the implications of the Provision, I will clarify the standpoint from which this evaluation takes place. In the next chapter I discuss legitimacy as a sociological framework for the critical analysis of law. I ask that if normative justification is key to a law's success, how should we evaluate this legitimacy? I suggest the approach of Habermas. In the remainder of the chapter I outline the basics of Habermas' social theory, before expanding on his theory of law and outlining how this relates to sustainability and corporate governance.

## Chapter 3: LAW AND CRITICAL THEORY

### 3.1 THE LEGITIMACY OF LAW

In modern society many believe that laws are valid when they are *'substantive and unambiguous'* (Edelman & Suchman, 1997:485). In Western Society rationality is closely linked to the *'goals of capitalism'* and thus laws are often evaluated on their propensity to allow *'rationally predicted'* outcomes (Freeman, 2008: 839-841). It would be naïve, however, to believe that because an action is deemed illegal by virtue of either statute or common law, that such action is no longer committed. Compliance is a particularly contentious topic in Corporate Governance (McBarnet, 2007).

In prescribing how we *'ought'* to behave, law is intrinsically related to morality: Emile Durkheim famously maintained that *'law [is] an example of the concretisation of social norms and values in society'* (Donoghue, 2009:55). Law's influence can be categorised into three domains: coercive power (through punishment and rewards); cognitive power (it presents the most sensible action) and normative power (the law appeals to our morals) (Freeman, 2008: 333). In reality legal influence is a combination of each of these powers (Edelman & Suchman 1997: 496-497) but most believe that normative legitimacy is key to its successful application (Tyler, 1990).

Sociology of Law attempts to investigate the clash between what is and what ought to be (Donoghue, 2009). As David Hume most famously noted *'ought'* and *'is'* are not the same and laws are *'not valid by virtue of their content'* alone (Freeman, 2008:330). Thus many believe that legal *'research should not examine in isolation practices and formal legal rules'* (ibid:52) and socio-legal studies seek to place law within a wider context: seeking to establish the conditions which drive people to obey the law (Freeman, 2008; Tyler, 1990).

Both mainstream CSR and organisation research have focused heavily on the positivist nature of current practices: concentrating on *'ideological functions'* with little regard given to the normative considerations of current corporate governance models (Scherer & Palazzo, 2007; Meisenbach, 2006:1100). Therefore it is an area ripe for further research and consequently an ideal starting point from which to evaluate s172.

Some legal theorists have considered law as a positivist discipline in which we adopt objective analysis of what the law says, however, this might encourage us to *'confuse legitimacy with efficiency'* (Outhwaite, 2009: 145). Critical theorists believe that objectivity in law is false: *'truth isn't outside power or lacking in power. Truth is a thing of this world'* (Foucault quoted in Baxter, 1996 : 450). They would argue that legitimacy based on the objective truth of modernity is the normative manifestation of the goals of the capitalist system (Callinicos: 2010).

Similarly a theory which supports the legitimacy of a law for its rationality of purpose and ignores the ubiquitous multiculturalist problem of universality (McBarnet et al., 2007) might be considered a *'sociological [theory] of law [which conveys a ] false realism that underestimates the empirical impact of the normative presuppositions of existing legal practice'* (McCormick, 1997: 734).

I agree with those who maintain that *'realities can be multiple and meanings ambiguous'* (Hodge et al., 2007:325). However, adopting such an epistemology -in which *'all knowledge is socially constructed'* (ibid) and we can objectively evaluate neither *'what is'* nor *'what ought to be'* - makes critical, yet constructive, legal research somewhat problematic. These somewhat nihilistic tendencies of critical social theory offer little scope for a pragmatic approach to issues of sustainability and *'some structure must be implemented for sustainable development to attain the [momentum] it needs to survive'* (Wironen, 2007:7). The prolific social theorist Jürgen Habermas offers a potential alternative theory.

## **3.2 HABERMAS' SOCIAL THEORY**

### **3.2.1 THEORY OF DISCOURSE ETHICS**

Continuing to support his predecessors *'concern with the dominance of instrumental reason'* (Outhwaite, 2009:19) Habermas does not outright reject the promise of modernity. Instead he believes that law should be *'socially effective'* and *'ethically justified'* (Freeman, 2007:868). He considers law as neither social facts (legal positivism) nor inherently moral (natural law) (Thomassen, 2010:115). Instead he seeks to find an alternative route "Between Facts and Norms" (1997) in which the *'legitimacy of the laws is down to the quality deliberations about the laws'* (Thomassen, 2010: 118).

Habermas seeks to consolidate the issues of subjective knowledge with universal morals, through development of the idea of 'Communicative Reason'. He believes that language is what distinguishes humans from nature and that our ability to communicate allows us to

participate in rational discourse, which, in turn, leads to ‘Universal Consensus’ (Thomassen, 2010). For Habermas communication is conducted through ‘Speech Acts’. Each Speech Act is subject to three ‘Validity Claims’: truth (a statement of affairs); rightness (moral intersubjectivity) and truthfulness (a statement of intentions) (ibid). Consideration of these Validity Claims help the listener to accept or reject the communicator’s argument (Finlayson, 2005:40). For Habermas human development is contingent on a constant progression towards mutual understanding (Outhwaite, 2009:57).

Habermas contends that our intersubjective communications occur within ‘The Lifeworld’: *‘our everyday world which we share with others ‘and from which we gain and cultivate social and cultural meaning (Finlayson, 2005:52-53). He therefore realises that Validity Claims are subject to personal experience and history and thus ‘Democratic legitimacy... cannot be grounded in the substantive ethical commitments of any particular community’ (Fraser, 2001:370). However, he believes that within specific circumstances (‘The Ideal Speech’ situation) rational debate - based on arguments not individuals - can flourish. A ‘Public Sphere’ in which every ‘citizen [has the opportunity] to deliberate freely and equally and in this way [form] their opinions’ (Thomassen, 2010:53) will allow rational discourse to occur.*

In other words he promotes a universally acceptable process of consensus building which he calls ‘Discourse Ethics’- rather than the imposition of one ethnocentric idea or goal. This consensus building allows citizens to install institutions based on *‘instrumental and strategic rationality’* which allow more efficient *‘material reproduction’* in society (Thomassen, 2010: 74). The efficient and self-steering institutions (‘The System’) are driven by the objective criteria of money (Anderson, 2005) which assist in managing the ever expanding Lifeworld. The System helps *‘ease the burden that falls to communicative discourse: they help hold society together’* (Finlayson, 2005: 54).

### 3.2.2 COLONISATION OF THE LIFEWORLD

As Habermas developed his theory, he realised that whilst *‘rationalization of the Lifeworld makes possible the emergence and growth of subsystems’* the *‘independent imperatives [of the subsystems] turn back destructively on the Lifeworld itself’* (Anderson, 2005:116). This Habermas terms ‘The Colonisation of the Lifeworld

The Colonisation occurs because money – the primary interest of The System – cannot be democratised (ibid) and thus, when the corporation (an actor in The System) ‘*enters the Lifeworld to exercise its free-speech rights, it [can be] expected to be fixated on the corporate bottom line*’ (Staats, 2004:593). Consequently it is difficult to see how ‘voluntary’ corporate responsibility based on intersubjectivity of goals and demands could ever exist from Habermas’ point of view.

### **3.3 HABERMAS AND LAW**

Instead Habermas believes that ‘*law is the mediator of the Lifeworld and System*’ (McCormick, 1997:735) which can ‘*protect areas of life that are functionally dependent on social integration through values, norms and consensus formation to preserve them from falling prey to the systemic imperatives of economic and administrative subsystems*’ (Habermas as quoted in Outhwaite, 2009:99). He believes that law can be both ‘*normatively rich and substantively rational*’ (McCormick, 1997:736) and can ensure maximisation of instrumental efficiency in The System, without undermining the ability of The Lifeworld to work towards mutual accord on moral values.

In a similar vein to his Discourse Ethics Habermas considers that law is legitimate as a reason of procedural formality rather than instrumental outcome<sup>3</sup>. He argues that ‘*the only regulations and ways of acting that can claim legitimacy are those to which all who are possibly affected could assent as participants in rational discourse*’ (Habermas, 1996: 458). Consequently he does not categorically reject the idea of law as a strategic implement (a social fact) but instead tempers its supposed objective application with a universally accepted procedure for its creation.

He reduces the law to neither instrumentality nor normative validity: in short his theory of law is ‘Between Fact and Norm’ (1997). It is this ‘transdisciplinary’ consensus- based approach to legality that, in my opinion, makes Habermas’ legal philosophy an interesting standpoint from which to evaluate law, and an appropriate and applicable theory for the field of sustainability science.

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<sup>3</sup> He does not consider the nature of the law important, except to the extent that it is imposed by a recognised body and that it ‘*can actually be enforced against deviant behaviour*’ (Habermas, 1996:116).

### 3.4 HABERMAS AND SUSTAINABILITY

The sustainability paradigm largely falls within 2 discourses; those who support the goals of modernity but encourage development in a sustainable manner (Ecological Modernisation for example); and those who believe that sustainable growth is oxymoronic and thus modernity is a fundamentally flawed concept (i.e. The Deep Ecology Movement). (Wironen, 2007). Undoubtedly the dominant discourse is that which encourages sustainable development: particularly in relation to corporate responsibility (Wironen, 2007, Meisenbach, 2006). Nevertheless much of sustainability science research is concerned with balancing these ‘weak sustainability’ practices with the normative considerations of more ‘dark green’ sustainability groups.

It has been argued that *‘a Habermasian approach provides the theoretical and practical means for addressing [this] communicative breakdown in such a way as to answer the critique of radical sustainability theorists (the anti-modern school) without abandoning the project of modernity’* (Wironen, 2007:36) His Discourse Ethics have been used as moral justification for increasing stakeholder dialogue in a corporate setting (Meisenbach, 2006) and have provided a basis for discussion on restructuring corporate social and environmental reporting (Lehman, 2001). Certainly when *‘his project is to develop a philosophy that can fully acknowledge the insights of post-modernism and cultural pluralism, while at the same time serve to preserve some form of reason as a guide to everyday practices’* (Brulle, 2002:3) it is possible to argue that Habermas seeks to understand the problems at the heart of sustainable business.

This approach is not without its critics. Habermas does appreciate a need for ecological preservation as *‘basic rights to the provision of living’* (Habermas, 1997:123) but some environmental philosophers suggest that his Discourse Ethics are too anthropocentric to sufficiently address the interests of nature (Brulle, 2002:6). Robin Eekersley argues that because the ‘natural world’ cannot communicate it is effectively excluded in an Ideal Speech scenario (Brulle, 2002). However, others have suggested that the exclusion of nature’s voice from Habermas’ theory is unimportant because *‘healing the rift between human beings and the natural world is not a matter of joining what once put asunder but of getting the relations between human beings right first’* (Dobson quoted in Brulle, 2002:15).

There are those, conversely, who also doubt the ability of Discourse Ethics to address the issue of relations between humans. One of the most popular critiques of Habermas’ theory is that it is too ‘utopian’ (Outhwaite, 2009): particularly in relation to law, to which he has been *‘accused of attaching a heroic quality’* (Freeman, 2008:869). Some believe that

he has underestimated the ability of corporate power to colonise The System, especially with regards to media control (Staats, 2004). Certainly the limits of Habermas' theory in promoting 'voluntary' corporate responsibility are well noted (Scherer & Palazzo, 2007). Whilst I do not think these critiques invalidate the use of Habermasian theory as a framework for critical legal analysis, they must be borne in mind.

### **3.5 HABERMAS AND CORPORATE GOVERNANCE**

Habermas has directly addressed neither environmental concerns nor corporate responsibility, but to my mind, he would agree that corporate responsibility cannot occur organically. He might be more inclined to support Scherer and Palazzo who conclude that the aim for CSR is not '*the creation of value based homogeneity*' but rather to '*enhance democratic control over an organization*' (2007: 1114). Habermas does not reject the idea of private law which allows citizens to '*seek and find happiness by pursuing their own private interests*' (Habermas, 1998:14) but he does think that the Public Sphere should set the rules of the game in which these interests can be pursued.

No studies have attempted to use a Habermasian theory of law to assess corporate governance legislation: this could be because in this theory he primarily concentrates on the constitution of public institutions. I think there is an argument that his theory should be extended to company law; especially if we recognise the growing domination of corporate actors in the Lifeworld (Staats, 2004: 116). Ward maintains that '*company law provides a very basic constitutional framework for the pursuit of profit*' (2008:19) and consequently I think illustrates Habermas' own observation that private and public law are intertwined (1996:392).

In this thesis I will therefore consider whether the Provision would be compatible with the democratic conditions required for the Ideal Speech situation. This is quite a wide application of Habermas' theory (such criteria usually only applies to constitutional laws governing public bodies) but I do not think it is an incompatible approach. Consequently in the subsequent chapters of this thesis I will review s172 of the Companies Act 2006 (as an example of legislation intended to shape corporate governance) and consider the potential consequences for UKFR. I will evaluate the current law and propose amendments which might make its application more successful in promoting sustainability. I then use Habermas' theory of law to critically evaluate both the existing law and my proposed amendments.



I do not debate whether corporate governance falls within the remit of private or public law nor do I wish to ruminate on the potentially wider implications of expanding Habermas' theory to UK company law. Instead I have chosen to consider s172 alone as I think this is an important test to establish whether '*existing institutional structures [can] bring about social and environmental reform*' (Lehman, 2001: 723).

## Chapter 4: METHODOLOGY

In this chapter I outline my research methodology and case study justifications, before more closely examining an example of corporate governance legislation: s172 of the Companies Act 2006 (see **Box 1** p32), which has been implemented to encourage more sustainable thinking by directors.

My research falls within two categories: legal research and a sociological study. Whilst the latter can be described as a largely qualitative study, legal research does not obviously fall within either qualitative or quantitative definitions. Traditional legal research – law as an empirical science – takes a positivist stance<sup>4</sup> which is somewhat contradictory to both my own ontology and that of Habermas. Therefore, I chose to analyse my empirical data from a socio-legal perspective. It also goes some way to explain the dichotomy between my strictly formulaic legal information gathering (in which I took an objective approach) and the critical approach I undertook in obtaining my information on UKFR. I will discuss the methodology and justification for each separately.

### 4.1 LEGAL RESEARCH

#### 4.1.1 JUSTIFICATIONS

In its promotion of Enlightened Shareholder Value (ESV)<sup>5</sup> the Provision cannot claim to be the only (or best) corporate governance legislation for sustainable thinking – the corporate governance model of many of the UK’s continental neighbours already promote a more pluralistic approach (Kagerman, 2004:111). However, s172 is the first time that such a multi-stakeholder consideration has been codified in UK law (Steinfeld et al. 2006). The Provision was seen as such a departure from the norm that it attracted much debate and was considered ‘*one of the most important and controversial provisions*’ in the Act (Morse et al. 2006:166). Its adoption has brought widespread criticism (Bruce, 2010:45) and it is interesting to consider the foundations of such criticisms, especially when initially the law

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<sup>4</sup> In that the effects are largely considered to be universal and morals are not taken into account (Freeman, 2008: 326)

<sup>5</sup> Enlightened Shareholder Value is a ‘*hybrid*’ between pluralism and shareholder value ‘*which maintains the primacy of shareholders but requires a long-term approach and permits directors to consider other interests as the best way of securing prosperity and welfare overall*’ (Fisher, 2009:11)

appears a welcome addition to UK Corporate Governance. In addition as my academic and professional background is in Scots law, I have a deeper and more widespread knowledge of the legal systems in which the law operates.

#### 4.1.2 RESEARCH METHODS

For the legal aspect of my research I adopted a primarily objective approach to knowledge building. I conducted a literature review of legal textbooks and articles which I used to support my reading in leading company law guides (Morse et al, 2006; Steinfeld et al, 2007; Walmsley, 2007), legislation and any existing case law. My findings do rely more heavily on commentaries and academic opinions that is usual in legal research (especially in a common law jurisdiction) (Smith, 2006) however this was a consequence of the infancy of the law.

Similarly whilst legal findings are usually presented in a prescribed systematic fashion, with distinctions made between judgements and legislation (ibid), so limited was the availability of legal sources on the Provision, that I have not made any hierarchical distinctions in my findings.

#### 4.1.3 LIMITATIONS OF THE RESEARCH

Beyond the limited availability of relevant cases and legal commentary, my research is also somewhat unorthodox in that I have largely chosen to ignore the different jurisdictions of the UK. Under normal circumstances research would be conducted on Scots law or that of England and Wales: each jurisdiction enjoying a different legal system. However, in my research, in order to broaden the availability of both legal commentary and number of potential interviewees, I chose to focus on the UK as a whole. This is less problematic in relation to company law because all jurisdictions fall under the Companies Act and so there are fewer opportunities for divergence. Additionally nothing in my research suggested that s172 would be interpreted substantially differently in Scotland.

## 4.2 EMPIRICAL RESEARCH: CASE STUDY OF UK FASHION RETAILERS

### 4.2.1 JUSTIFICATIONS

Fashion is emblematic of our consumer culture. Perhaps the original purveyor of planned obsolescence (Yurchin & Johnson, 2010:62), every year fashion gets faster<sup>6</sup>, cheaper (Siegle, 2011) and more competitive: with the result that some see the industry as competing in a ‘race to the bottom’ (Jackson & Shaw 2008: 153). Unable to compete on anything other than price, many companies advocated the maxim ‘pile it high, sell it cheap’ (ibid: 147).

‘Fast Fashion’<sup>7</sup> brands now account for 1/5 of the UK clothing market (DEFRA, 2011b) and the average consumer now purchases 34 items of clothing per year (up from 19 items in 1997) (Centre for Sustainable Fashion, 2008: 16). This situation has profound effects on our environment. Textile and apparel production is one of our most polluting industries; on average production a kg of textiles requires 50 litres of fuel and 2000 litres of water (Brand et al, 2008:132)<sup>8</sup>.

The rise in consumption has also seen an increase in landfill waste (Morgan & Birtwistle 2009). In the UK about one billion tonnes of clothing is to landfill each year: about 50% of all clothing waste (ibid: 190). Once in landfill the natural textiles biodegrade producing climate changing greenhouse gases whilst the synthetic fibres fail to break down and accumulate as years of wasted resources (Fletcher, 2008)<sup>9</sup>. DEFRA estimates that the 1.5-2 million tonnes of waste clothing in the UK in 2006, represented 70 million tonnes of waste water, 989,000 tonnes of oil and 3.1 million tonnes of CO<sub>2</sub> equivalent emissions (2008).

The most obvious solution would be for individual consumers to ‘buy less’ but this maxim seriously misunderstands our relationship with clothes (Fletcher, 2008: 117-120) as well as underestimating the power of marketing and business to encourage ‘*extreme consumption*’

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<sup>6</sup> Zara changes its range 17 times per year (Jackson & Shaw, 2008: 89)

<sup>7</sup> Fast Fashion: ‘*making large profits by selling low-price clothing to shoppers seeking something new to wear each week*’ (Morgan and Birtwistle, 2009:190)

<sup>8</sup> Although these figures vary greatly both between textiles and places of production: cotton is notoriously water expensive, whilst manmade fibres use much more oil (Fletcher, 2008).

<sup>9</sup> Fast Fashion (which uses more synthetic materials) is more likely to be sent to landfill (Fisher et al, 2008)

(Yurchisin & Johnson, 2010:143). In addition the fashion industry offers 26 million jobs worldwide and contributes \$1, 334.1 billion to the global economy (FFTF 2010).

Most agree that business must play a key role in creating sustainable fashion. Until recently, focus has been primarily on the design and production side of the industry, with little consideration given to consumption and the resulting waste: Fletcher (2008) describes this as the *'elephant in the room'* (p117). In my opinion it offered an ideal opportunity *'for a critical test of a significant theory'* (Yin, 2003:41).

#### 4.2.2 RESEARCH METHODS

For my empirical data-collection I used a mixed-method approach, however, I chose to predominantly focus on qualitative methods. I contacted forty-six UKFR, first by telephone and then up to three times by email. In these emails I explained my research (although not disclosing its exact nature, in order to limit any bias) and suggested anonymity of response at their discretion, on the basis that detailed information about the topic and the promise of anonymity have been shown to improve response rates (Le Blanc & Schwartz, 2007). I have since decided that all of my interviewees will remain anonymous as it is not my intention to provide a critique of individual retailers but rather an industry overview.

I conducted semi-structured interviews (for my interview questions see Appendix 1) with four company directors and one sustainability manager for UKFR<sup>10</sup>. Two of these interviewees were 'gatekeeper' contacts (ibid: 848) and three I arranged by cold-calling companies. I also had an 'email interview' with a representative from DEFRA.

This was slightly fewer interviews than I had originally planned: consequently I produced a short summary questionnaire which incorporated some of the ideas in my interview questions. I endeavoured to make the questionnaire quick and readily accessible (Gordon, 2002; Collier et al. 2005) and I followed recognised frameworks to encourage participation (Weimiao & Zheng, 2009; Bosnjak & Tuten 2001). In addition to distributing the questionnaire to the original companies, I also posted it on the 'Linked-in' forums of industry specialist magazines 'Drapers' and 'The Retail Week'. I received only one response.<sup>11</sup> I am reluctant to read too much into this response rate but as people did not

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<sup>10</sup> My 'eco-fashion' label is an online retailer. See Appendix 2 for Interviewee Details

<sup>11</sup> This response, being from a non-UK based company- was unusable.

even attempt to access the questionnaire, it suggests that it is the topic that was of no interest or perceived importance to the executives, rather than a failure of questionnaire design (Bosnjak & Tuten, 2001).

‘Board research’ is notoriously difficult to undertake (Le Blanc & Schwartz, 2007; Guerra et al. 2009) and, on reflection, I think the spectrum of directors I spoke to, in combination with my other research gave me sufficient data to allow me to extrapolate trends and contribute to corporate governance research.

To support the information from my interviews, I tried to develop a greater understanding of discussions of sustainability within the fashion industry. I undertook a brief survey of the CSR and environmental policies of the forty-six companies (Appendix 3 shows a table of results). I also attended a conference on ‘Towards Sustainability in Fashion and Textiles’ run by the Copenhagen School of Design and Technology (KEA, N.D.) which featured a number of speeches by academics, business professionals and designers. Finally I undertook a ‘literature review’ in which I considered academic papers, consultancy reports and media discussions.

#### 4.2.3 LIMITATIONS

I have no professional experience in fashion, and my interpretation of the industry is, of course, shaped by my background. I have intended to keep an open mind, however, undoubtedly (and certainly in relation to my selection of companies<sup>12</sup>) bias will have occurred. This is particularly expected in qualitative research where reproducibility is difficult to ensure (Bryman, 2008).

I did not investigate the background of my interviewees, except to the extent of establishing their knowledge about sustainability. A lot of research has considered how board composition can affect corporate decision-making (Guerra et al: 2009) and it is certainly within reason that the social background and characteristics of my interviewees may have shaped their responses.<sup>13</sup>

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<sup>12</sup> I chose companies that I considered well known High Street Brands. By which I mean retailer with online or High Street stores which sell their own brand of clothing.

<sup>13</sup> All of my interviewees were men, given that past research has shown that men and women have different approaches to risk, money and sustainability (Caretta, 2010) this could be an area for further research.

I chose to look only at free information on ethical fashion reporting (i.e. those available on the company websites). Company accounts are available from Companies House<sup>14</sup> and I did purchase the accounts for my interviewee companies. However, I decided that to buy accounts for all 46 companies was excessive – especially as I would have had to buy multiple accounts to establish company structures. This might mean that I have over-estimated the uniqueness of those companies who have publically available accounts which included environmental reporting<sup>15</sup>.

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<sup>14</sup> The UK Company Directory

<sup>15</sup> Although it should be noted that not all publically available accounts include information on environmental risks: one company optimistically reported “*The Group does not operate in a business sector which gives rise to significant pollution, but the Board recognises that the business could have an impact on environment*”.

## Chapter 5: THE LIMITS OF s172

Whilst it has been claimed that s172 encourages long-term thinking from directors (DTI, 2007) the Provision has come under a number of criticisms from several sources (Nakajima, 2007:2; Villiers, 2011). The Provision is just one part of Chapter 2 of the Act (s170-179) which seeks to clarify directors responsibilities. For certain companies (those with a turnover of more than 5.6 million) the Provision is to be read in conjunction with s 417 which requires directors to produce a business review with a risk assessment in relation to each of the factors in s172.

### Box 1: The Provision

#### Section 172 Duty to promote the success of the company:

A director of a company must act in the way he considers, in good faith, would be most likely to promote the success of the company for the benefit of its members as a whole, and in doing so have regard (amongst other matters) to

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

The Act is the '*first time [directors'] duties are enshrined in statutory form*' (Mortimer, 2009: § 9.01). The duties, based on those at common law, are not exhaustive, are open to interpretation and may change over time (Mortimer, 2009). In this sense whilst s172 expands on the criteria that directors must consider (e.g. environment and community *ibid* §11.21) it does not set strict rules for directors to follow. It is assumed that interpretation of the Provision will follow the established common law principle that '*the duty [of a director to a company] is a subjective one... the question is whether the director honestly believed that his act or omission was in the interests of the company*' (Jonathan Parker J in *Regentcrest plc (in liquidation) v Cohen and another* [2000] All ER (D) 747 § 120).

Ambiguity is just one of a number of criticisms that have been levelled at the Act. In the remainder of this chapter I will consider this i) ambiguity of the extent of a directors'



duties, in addition to the issues of ii) promoting the success of the company; iii) the weight given to each factor and iv) documentation of decisions'. I will outline the legal implications and then discuss the potential outcome for environmental management in UKFR.

It should be noted at this point that only 1 of my 4 director interviewees (Interviewee D) was fully aware of his duties under the Act. Interviewee C alluded to the fact that his bosses had held discussions surrounding the Act but had dismissed it as inconsequential: *'no ones ever been pulled up on it'*. This finding offers more interesting for my eighth chapter and so, for the purposes of this chapter, I have presumed that the directors are fully aware of the existence of the Provision

## 5.1 AMBIGUITY OF THE REQUIREMENTS

It has been argued that the required considerations in s172 are *'mandatory but not exhaustive'* (Mortimer, 2009: § 11.14). The Act does not set objective criteria as to the extent of these considerations but instead grants *'unfettered discretion'* to the directors (Keay, 2007:107). During implementation discussions, then Minister of State for Industry, Margaret Hodge explained *'the words "have regard to" mean "think about" they are absolutely not just about ticking boxes'*. (Hansard 2006a). This follows the common law which has long advocated that *'the [directors] must exercise their discretion bona fide in what they consider- not what a court may consider – is in the interests of the company'* (L Green MR in Re Smith & Fawcett [1942] Ch 304 p306).

To understand how the courts might interpret bona fide discretion we can look to discussions on a director's duty to exercise reasonable care, skill and diligence<sup>16</sup>. A director's duty of care is largely considered to be both objective (that of the ubiquitous reasonable man) and subjective (where a director's expertise is beyond that of the average director (s)he will be held accountable to a higher standard) (Mortimer, 2009)<sup>17</sup>. Directors will not be considered in breach of their duty for a mere error of judgement (ibid). In order to appreciate how this interpretation might work in practice for environmental management in UKFR it is necessary to consider the level of knowledge of UKFR directors.

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<sup>16</sup> Codified in s174 of the Act (see Appendix 4)

<sup>17</sup> This requirement is codified in s214(4) of the Insolvency Act 1946 (see Appendix 4).

Studies have shown that a large number of executives consider sustainability as important in their business (McKinsey & Co. 2010). In the fashion industry 72% of companies maintained that sustainability was important (Centre for Sustainable Fashion, 2008:19). It has been argued that sustainability is still largely considered by business as meaning environmental management (Crane & Matters, 2007: 25) and for two of my interviewees this was the case<sup>18</sup>. Conversely the majority of companies do not have someone responsible for sustainability (Centre for Sustainable Fashion, 2008:24) and very few publicise any environmental policies. In the forty-six companies I examined only twenty-five had information on their environmental actions on their website (Appendix 3).

My own interpretation is that a number of directors fail to appreciate the consequences their industry has on the environment. In general companies tend to focus on the production process and this also appears to be the case in fashion (Fletcher 2011). Little thought is given to post-consumer waste (Fletcher, 2008)<sup>19</sup>. I asked my interviewees what areas they considered most important and waste did feature heavily, however, this was rather from a production perspective than relating to the number of garments sold. The predominant areas of concern for my interviewees were labour rights and to a lesser extent supply chain management. This is a recognised trend in fashion (Ellebæk Laursen, 2011).

My interpretation of UKFR is that it is very difficult to pinpoint the level of knowledge of the ‘reasonable’ director. The majority of companies receive their information on sustainability issues from the media (Centre for Sustainable Fashion, 2008:19) and consequently it is possible that – on average- their knowledge of sustainability is not that much greater than the average citizen<sup>20</sup>. As studies have shown that understanding of sustainability in fashion is low (Fisher et al, 2008), it is fair to speculate that courts might not hold directors’ skill and knowledge of such issues to a very high standard.

## **5.2 PROMOTING THE SUCCESS OF THE COMPANY**

This wording is potentially the most controversial in the Provision. Prior to enactment many discussions were held in relation to the benefits of shareholder value versus

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<sup>18</sup> When asked whether his definition of sustainability went beyond environmental management Interviewee B answered ‘*slightly more encompassing but principally environment*’

<sup>19</sup> The DEFRA Roadmap has been criticised for this (ENDS 2010)

<sup>20</sup> 3 of the 5 companies I interviewed had never heard of the DEFRA Roadmap or any other sustainability initiative in fashion, even when prompted (I used the example of the Centre for Sustainable Fashion)

pluralism (Mortimer, 2009). In choosing *'the success of the company'* shareholder value appears to have won the debate (Villiers, 2010:11). As a company is a representation of the collective aims of its shareholders, their definitions of success are considered synonymous. Whilst in theory the success of a company can mean anything, it is thought that *'for a commercial company, success will usually mean long-term increase in value'* (Lord Goldsmith in Hansard, 2006b).

If a director fails to consider a factor under s172, the company (i.e the shareholders) can raise a derivative action against the directors for any loss appreciated by the company. Derivative actions are outlined in Part 11 of the Act and can usually only be used if the majority of shareholders agree to raise an action. This is because the action is raised on behalf of the company and not as an individual shareholder (Mortimer, 2009)<sup>21</sup>

Initially it was thought that a more encompassing stakeholder accountability could lead to *'vexatious claims'*: particularly from environmental activists.(Reisberg, 2009:17). However the requirement to raise a derivative action has put paid to this idea<sup>22</sup>. It appears that most law firms (Loughrey et al, 2008) and companies (Herbert Smith, 2006) are unperturbed by a suggestion of an increase in legislation<sup>23</sup>.

In most cases where there is no threat of sanction a law will have limited effect (Tyler, 1990). The risk of derivative action depends largely on the company structure, something with my limited number of responses it was difficult to investigate in my research. Three of the companies I interviewed were co-owned by the director. Whilst the rules on minority shareholders do allow for derivative action in this instance, it is difficult to envisage a scenario in these smaller companies where a director would be sued for failure to consider one of the s172 factors. The exception might be where an employee shareholders scheme was in place (as was the case with one of my interviewee companies).

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<sup>21</sup> The exception to this rule arises where a shareholder minority can claim discrimination or an individual shareholder can *'demonstrate a) a breach of duty owed to him personally and b) personal loss separate and distinct from that of the company'* (Mortimer, 2009 §21.08).

<sup>22</sup> In the limited number of cases reported, some have already failed procedurally ( Bruce, 2010: 238)

<sup>23</sup> A survey by Herbert Smith (2006) of companies found that 71% had not purchased more Directors and Officers Liability Insurance and despite some calls from experts that they should review indemnity insurance (Beale, 2007) uptake of liability insurance remains low (Smerdon, 2007) which suggests that few companies expect claims to arise.

In addition, the clause also suggests that the shareholders are less short-term orientated and monetarily driven than directors, which may not be the case (Loughrey et al. 2008). Two of my interview companies were owned or operated by venture capitalists whose primary interest in the company – one might expect – is profit: *‘at the end of the day the Venture Capitalists are there to make money’* (Interviewee C)<sup>24</sup>. This is not the interpretation I received from the directors themselves who all focused primarily on the wellbeing of their employees and the moral imperatives that encouraged them to undertake their jobs ethically. This supports the finding that environmental performance has only a slight correlation with executive pay (Cordeiro & Sarkis, 2008). In short there is little to suggest that directors do not already act in the best interest of the company and moreover in the interests of multiple stakeholders. I asked the question ‘to whom do you owe a duty of care in carrying out your duties?’; without exception my interviewees answered their employees and customers. Nobody mentioned shareholders and only one director mentioned himself and it was not in relation to financial compensation. Interviewee D stated *‘I built this job in order to reflect the importance to me of right livelihood, of living and earning my living in a way that I feel is in accordance with my principles.’*

Whilst it has been argued s172 encourages ESV, many have claimed that this is a serious limitation on the consequences of the Provision (Fischer, 2009; Villiers, 2010). It has been argued that the law was implemented not as a means of encouraging pluralistic thinking but rather to ensure that directors did not profit at the expense of the company (Fischer, 2009; 14).

### **5.3 THE WEIGHT GIVEN TO EACH FACTOR**

The Provision does not offer any guidance as to how each factor should be ranked: so directors must personally decide whether to give credence to long or short-term consequences (Mortimer, 2009 §11.21). The Attorney General Lord Goldsmith stated that *‘we want the director to give such consideration as to the factors identified as is necessary for the decision that he has to take and no more than that’* (Hansard, 2006c). Recent case law suggests that a director is given ultimate discretion as to which factor they consider most pertinent in a given situation (*Shepherd v Williamson* [2010] All ER (D) 142). I enquired as to which aspects directors might consider more in their decision-making in UKFR.

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<sup>24</sup> More and more UKFR are owned by large holding company which seeks to vary their portfolio in order to reduce financial risk and maximize profit (Jackson & Shaw, 2008).

From my interviews I would conclude that employees and labour rights are likely to be given greater credence than, environmental or community considerations (with the exception of Interviewee D who appeared to rate both very highly). In general environmental factors were not considered very important: perhaps because the directors did not deem them a risk to their business. According to my interviewees, consumer concern is still very low in relation to environmental impacts of products (something that is supported in the literature). Similarly none of my interviewees suspected impending government legislation on environmental matters which would have relevance for their business: this seems like a reasoned assumption as current government approaches appear to be based entirely on voluntary procedures (DEFRA, 2010).

Environmental considerations also varied in relation to different points in the process. Whilst LCAs are becoming more common in fashion they usually only consider the initial production stages of the supply chain: with design and consumption stages considered less important. For example 'Made-by' - a prominent consultant and LCA specialist in fashion retailing - focus only the early stages in the production process (Tobiasson & Kviseth, 2011).

Weighting of considerations appears to rely heavily on the short or long-term consequences of the factors. Fashion is a very fast business and long-term thinking is not supported by the system: *'short-term tactical pricing is a major part of fashion branding'* (Jackson & Shaw: 135). As I mentioned previously prices in fashion are dropping and *'when prices are low'* there is little drive to innovate (Fletcher, 2008:44). So whilst work is being done on developing more durable and sustainable textiles, as long as prices of virgin materials remain low there is little incentive to sell more sustainable products (ibid). This short-termism also limits the availability of negative feedback of environmental information (Cataldi et al. 2010). This means that if that even if directors wished to consider ecological effects the data is not available for them to do so: coherent and comprehensive environmental information is not widely available (Fletcher, 2008). This is particularly problematic for smaller companies who do not have the resources to dedicate to voluntary environmental information gathering (Perry & Towers, 2009). One of the smaller of my interview companies acknowledged that they just do not have the manpower to devote to considering the environmental impacts of their business (Interviewee A).

In summary, the highly competitive and complex nature of fashion retailing encourages short-term thinking and management (FFTF, 2010). Consequently there is little suggestion that those factors which might have either more long-term or less readily

identifiable economic consequences (i.e. environment and community) would ever take precedence over short-term financial gains.

## 5.4 THE DOCUMENTATION OF DECISIONS

With the exception of s417 (which only applies to larger companies) there is little advice given to directors on how they should document this decision-making process (Mortimer, 2009). It has been suggested that *'lip service'* is insufficient (Smerdon, 2007:91) and that the provision will only encourage a larger paper trail (Nakajima, 2007) but Margaret Hodge maintained that *'the clause does not impose a requirement on directors to keep records... in any circumstances which they do not now'* (Mortimer, 2009: §11.37). This ambiguity has led to complaints that the Act does not offer clarification on directors duties (Beale, 2007). Some have argued that without stricter criteria the business review will become *'self-serving and vacuous'* (Davis in Copp, 2009:20) serving only to reduce the liabilities of directors (Copp, 2009). It is also not difficult to envisage those situations in which public disclosure of the risks might not be in the interests of the shareholders (ibid).

There is encouragement towards more transparency in social reporting in the UKFR (DEFRA, 2010). Although criticism has been made that such reporting is currently voluntary (ENDS, 2010). Whilst some of the companies I looked at do have reports available online, this is not a comprehensive trend. Many of these CSR statements or reports did not include any environmental information (See Appendix 3)<sup>25</sup>. Those with the most comprehensive reports tend to be eco-orientated retailers or publically limited companies. The latter may be a consequence of the Act but may equally be attributed to any number of drivers<sup>26</sup>. If s172 does encourage more transparent reporting then the effects are limited.

It appears that s172 lacks potential to really encourage sustainable thinking by directors in UKFR. Does this mean that Habermas' theory is incorrect and that law is not the answer? Possibly not: in the next chapter I will discuss those changes that I think might make s172 more effective. I will then consider whether these amendments fit with Habermas' theory of legitimacy and the consequences this could have on the law's effectiveness.

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<sup>25</sup> Even fewer published specific information on waste.

<sup>26</sup> Including the current UK Pension laws which require social responsibility reporting from all pension managers in relation to scheme investments (Bruce, 2010:376).

Habermas considers the legality (legal enforcement of the law) an essential component of his theory of law (Thomassen, 2010). Any alternations which serve to make the law more enforceable would therefore presumably be welcomed. However, I will also consider how these ‘improvements’ sit with Habermas’ theory of Discourse Ethics, as I maintain it would be remiss to presume that Habermas would support any law that undermined this principle: *‘a legal order... owes its legitimacy to the forms of communication which are essential for [it] to express and preserve itself.*’ (Habermas, 1996:409). Taking the four critiques of chapter 5, I will suggest amendments to two areas: expansion of locus standi and increase in reporting.

At this point I should acknowledge that whilst I have focused on s172 as a means by which to encourage long-term decision-making in a company, that is not to suggest that the Provision is some kind of panacea. Gunningham and Sinclair (1999) state that *‘single strategy approaches are misguided’* (p 50) and I agree. The effectiveness of individual legislation is very much dependent on the society in which it operates and a ‘mixed-strategy approach’ (ibid) is arguably more effective in encouraging good environmental management. In this chapter I discuss those amendments which I think might make s172 more consequential and this will require looking at the system in which s172 stands. Although I highlight areas which might hinder the effect of the Provision, I do so to suggest issues for further reflection and I do not discuss the changes to other legislation that might be required; the latter being outwith the scope of this thesis.

### 6.1 EXPANSION OF LOCUS STANDI

Under the Act shareholders are the only stakeholders who have title to sue the directors for failure to consider the factors in s172. The decision to limit locus standi to this group was a direct consequence of the widespread support for ESV (Mortimer, 2009 § 11.02). However, as discussed in chapter 5, this decision probably means that few claims will ever be raised against the directors. Whilst I acknowledge that some believe a pluralist approach would have brought *‘economic disaster’* (Copp, 2009:21), I support the reasoning that those who are most likely to bring about an action are *‘those who live locally [to production] or are an employee’* (Fischer, 2009:9).

In theory ESV is closely connected to ‘*maximisation*’ of the interests of multiple stakeholders (Ho, 2010:19) but some have argued that ESV is effectively ‘*shareholders first*’ (Villiers, 2006:10). Shareholders are generally considered to be primarily financially interested in the company: ‘*for most people who invest in companies, there is never any doubt about it – money, that is what they want*’ (Lord Goldsmith in Hansard 2006b). Other stakeholders tend to have a wider range of interests in the company (see **Box 2.**). ESV only works when shareholders adopt long-term thinking (Loughrey et al, 2008:107) which is particularly an issue in those companies where shareholders adopt a ‘trader mentality’ (Villiers, 2010:18)

**Box 2: Table of Stakeholder Interests**

Type of Shareholder	Possible Principle Interest
Employee	wage; job security; personal development; working conditions
Director	job security; status; personal power; growth of the organisation; profitability
Shareholder	market value of investment; dividends; security of investment; liquidity of investment
Creditor	security of loan; liquidity of investment
Supplier	security of contract; regular payment; growth of organisation
Society	safe products; environment; equal opportunities

(adapted from Worthington & Britton, 2006)

Some maintain that there are few stakeholders who are concerned directly with the environment (Villiers, 2008: 214). Alternatively it could be argued that certain stakeholders are more interested in the environment than others. Public companies can have ‘*limited if any regional or national loyalties*’ (Parkinson, 1993: 264) whereas suppliers and producers who operate in a local community might be more inclined to ensure limitation of negative environmental effects (Gunningham et al. 2003). In the UK fashion industry most production is conducted overseas, and shareholders rarely feel the consequence of poor environmental management (Fletcher, 2008).

Similarly employees are arguably more likely to have long-term visions for the company; most people want to work for a company with some integrity (McBarnet, 2007:19). It might



also be presumed that employees would like to be associated with business that produces quality products. Adam Smith argued that what shapes our actions are the judgements of our peers and local community (1759); most people's friends know who they work for but few know their associates' stock portfolios.

Additionally studies suggest that green-collar graduates could bring new ideas and information to the business (Centre for Sustainable Fashion, 2009). Employees are conscious of the day-to-day running of the business and could provide useful reminders to management of their duties to consider all factors in s172. This only works if the employees are listened to by executives. I asked Interviewee C whether there was more understanding of sustainability at lower levels in the his company: he said *'there is an understanding of it... but people I talk to always seem slightly disillusioned. They are not empowered to do anything about it in their daily jobs... there is just not the tools or opportunity'*.

It could be argued that customers should be given title to sue: as the group that probably has the most interest in limiting the effects of marketing and mass production. However, financial sustainability is also key to a company's longevity and customers have very little interest in this. Consequently my suggestion is not to expand locus standi to include all stakeholders but rather to extend the duty of care of directors to those with more long-term interests than the trading shareholder. Other critiques might maintain that widening the scope of those entitled to sue would lead to a rise in vexatious claims, however, keeping the two-part test currently required for derivative actions might go some way to absorbing these actions (Mortimer, 2009).

Many directors already engage in multi-stakeholder dialogue (Crane & Matten, 2007: 185) and the companies I interviewed highly rate the opinions of their employees and customers. However, managers will rank stakeholders on power, legitimacy and urgency (Mitchell et al quoted in Crane & Matter, 2007: 185), as s172 grants power to shareholders only: with their rights to sue, shareholders may have a louder voice. Given that little consensus exists in relation to short-term economic benefits of CSR (Gunnigham et al, 2003: McKinsey & Co, 2010), inclusion of stakeholder interests with long-term views could potentially result in more responsible and environmentally sound decision-making.

## **6.2 INCREASE IN REPORTING**

Under the current legislation only certain companies are required to report 'the risks' in relation to the factors under s172. These reports are therefore primarily produced for

public companies and thus generally focus on financial risk. It could be argued that the annual requirement of the reports (or Business Reviews as they are called in the Act) perpetuates the short-termism that plagues business; it has been said that the demands of quarterly reviews discourage directors from adopting the long-term vision required for a sustainable company (Bisoux, 2010).

None of my interviewees were particularly worried about liability under future legislation. Nor were they perturbed by potential loss of business or bad press. In this sense the financial risks to the business are vague in at least the medium term. However, this does not mean that the environmental risks are also low. Many people (including one of my interviewees) argue that UKFR will not consider the environmental consequences without further regulation (FFTF, 2010; Interviewee C).

On the other hand, none of my interviewee directors wanted more regulation, already finding the existing legislation over-burdening. This supports the consensus that environmental legislation is 'ad hoc' 'random' & 'separate' (Bruce, 2010:381) and fails to introduce systemic environmental management. Particularly in an industry as diverse as fashion where it is difficult to introduce universally applicable standards (DEFRA interview).

One option might be to require companies to self-report, not only on the business risk to the company, but also on the environmental and social impacts associated with their business operation. This could increase transparency and communication between business and society. This would have profound consequences on the way in which business develops. Companies which rate highly on the FTSE Sustainability Index do not perform particularly well financially (McBarnett, 2007:26). Nevertheless it might encourage companies to be more open and honest in their dialogues, particularly with regard to the issue of waste.

Economies of scale are important in fashion (Jackson & Shaw, 2008: 70) and large companies are able to spend more on 'sustainable' schemes and initiatives. Marks and Spencers' (M&S) is seen as the flagship for sustainable retailing in the UK; their Plan A scheme was mentioned by all of my interviewees<sup>27</sup>. One of their most commended initiatives is their partnership with Oxfam, which sees customers receive a £5 voucher in

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<sup>27</sup> I agree that M&S does have one of the most comprehensive sustainable strategies on the UK High Street (Marks & Spencers, 2011)

exchange for any M&S clothing taken to the charity shop. Clearly smaller businesses would not be able to afford such a scheme, but it is an innovative way to ensure more clothes are sent to charity shops than to landfill. What it does not take into account is that Marks & Spencers accounts for 12.7% of clothing bought into the UK today and can afford this initiative thanks to the size of its operation (*figure from 2006*. Jackson & Shaw, 2008:19) The Oxfam scheme might actually exacerbate consumerism by promoting sales at M&S stores (the £5 voucher can only be used on purchases over £35).

The requirement that companies publish information on environmental affects, not only increases transparency to reduce this type of green-wash, but also allows society to see why companies have adopted such an approach. Some argue that voluntary reporting of CSR issues (including the environment) has benefits (Caby & Chousa, 2006). Others maintain that this reporting can never go beyond that which is clearly financially rewarding (or instrumentally rational) (Lehman 2001: 728). Habermas would agree that we need access to information (that might be potentially profit damaging) to allow fair and educated discussions to occur in the Lifeworld. The theory of Discourse Ethics requires conversation in which ideas are supported by rational arguments for our normative decisions (Lehman, 2001). This conversation is missing in retail.

We know that directors understand financial decisions but most have less experience in considering the environmental consequences of their actions. By requiring environmental impact reporting, we can help expand the rationalisation of risk beyond financial considerations and could help build trust in organisations' reporting by allowing consumers to effectively evaluate Validity Claims.

The form which this information could take is debatable, however, if the information was published on an annual basis there would incentive for companies to actively try to improve their environmental reports<sup>28</sup>. This could, for example, lead to more transparent labelling . Currently consumers are required to evaluate on price alone: studies show that price is still the main driver for purchases (Jackson & Shaw, 2008). Labelling is notoriously basic in the fashion industry (V&A, N.D.) and there is no globalised standard for organic fabrics for example (Tobiasson & Kviseth, 2011). If there was a requirement to list the 'ingredients' in a t-shirt, then organic fabrics might become more attractive.

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<sup>28</sup> This is one example where the law must work in conjunction with other 'licences'. The effectiveness of any reporting would require active scrutiny and participation from media and NGOs: something Gunningham et al (2003) feel is necessary for the 'social license to operate' (p35)

Similarly a t-shirt might only cost £5 because the company has produced thousands of them. If a company was required to identify the number of clothes of each design (as occurs in limited edition prints of paintings or books for example) this might not only encourage exclusivity as added value<sup>29</sup> but could also help consumers think about why their clothes are so cheap.

Accounting requirements give companies an annual incentive to consider their financial bottom line. Annual environmental reports could provide an incentive to companies to improve the triple bottom line: ‘*if fashion companies had to take responsibility for the quantities they produce then I think we would see a new way of thinking about fashion*’ (Suzanne Lee in Brand et al. 2008:101).

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<sup>29</sup> Many high street retailers already offer ‘limited edition ranges’

## Chapter 7: LEGITIMACY AND THE LAW

In this chapter I analyse the legitimacy of the law. Legitimacy is connected to successful compliance with a law (Tyler, 1990) and each can offer indications of the other's success. However, Habermas' concept of legitimacy is more procedural in definition: *'the only law that is legitimate is one that could be rationally accepted by all citizens in a discursive process of opinion and will-formation'* (Habermas, 1996:135). I will argue that s172 puts too much pressure on directors to make societal decisions and so is unjust, undemocratic, and therefore cannot be considered legitimate.

The perception of legitimacy is central to regulatory compliance. People are less likely to abide by laws that they feel are unjust (Tyler, 1990). One can evaluate the legitimacy of a law by consideration of its effect. The problem with this approach is that it is based on the normative considerations of individuals rather than society at large. When legitimacy is based on outcome alone, there is always a chance that some groups in society will not agree with that goal, not consider the law legitimate and thus be less likely to comply with regulation.

Alternatively we can consider legitimacy from a procedural perspective. This is the approach advocated by Habermas who maintains that we must consider the manner in which a law was created.

Using Habermas' theory that *'the only regulations.... that can claim legitimacy are those to which all who are possibly affected could claim legitimacy'* (1996:458) I have tried to evaluate whether my proposals would be considered legitimate. To a certain extent this is a contradictory exercise; a central component to both Habermas' theory of Discourse Ethics and law, is that universal values and legitimacy must be construed within a rational dialogue and not by individual objective theorising such as that proposed by John Rawls (1999). Consequently I am not attempting to pronounce a universal declaration on the legitimacy of the Provision but rather present my own, rationally supported arguments, grounded in an empirical case: that of the UKFR.

Before I consider the legitimacy of my amendments, I will briefly discuss the legitimacy of the Provision as it currently stands.

## 7.1 LEGITIMACY OF EXISTING s172

As I have previously discussed, s172 can be construed in two ways; as protection for shareholders or to encourage sustainable thinking. I have addressed the legitimacy of both.

### 7.1.1 THE PROVISION AS PROTECTION FOR SHAREHOLDERS

The current requirements of s172 are limited and arguably serve only to ensure that directors cannot use companies to make short-term personal economic gains at the expense of the shareholder. The backlash to both the economic crisis and corporate scandals such as Enron would suggest that this is a widely-accepted, if not universal norm (CECP, 2010).

None of the directors I interview commented on their own success as a goal and there are many examples where directors do consider the implication of their actions on the future success of the company (Bisoux, 2010). If s172 was designed solely as a mechanism to regulate relations between directors and shareholders then I think both stakeholders would readily concede its legitimacy. Other stakeholders, including employees and those in the supply chain, would also presumably accept the notion that directors should not profit from mismanagement of the company. It seems to be a law grounded in moral consensus.

### 7.1.2 s172 AS ENCOURAGING SUSTAINABLE THINKING

If, on the other hand, s172 was implemented to improve '*long-term sustainable success*' for companies (as suggested by Alistair Darling (DTI, 2007)) and the Provision was designed to promote the ideas inherent in ESV then the legitimacy might be more open to dispute.

Habermas thinks that legitimacy comes from a process of law-making that everyone affected by the law agrees to, in short he supports democracy. Whilst in theory s172 was enacted through a democratic process, in actuality this process is increasingly subject to the criticism that it suffers greatly from the over-influence of business (Korten, 1996). For reasons previously discussed it appears the law is designed to give primacy to financial success of the company, which may actually encourage short-termism and even be

contrary to the natural inclinations of directors, It could therefore be argued that this law perpetuates the colonisation of the Lifeworld.

Despite criticisms that he fails to account for the effect law can have on cementing the power of the system over the Lifeworld (Outhwaite, 2009:148), Habermas' legal theory does, in part, account for this. Law, for Habermas, is two-fold and includes both materialistic validity and normative procedurally. He not only asks is the law procedurally legitimate but also did it achieve what it set out to do. As there is no real enforcement mechanism, if the role of s172 is to promote sustainable thinking in the boardroom then it has failed.

## **7.2 HABERMASIAN ANALYSIS OF THE AMENDED PROVISION**

In chapter 6 I made suggestions which might improve the likelihood of s172 achieving this goal. If these amendments are made, I think the Provision will become more materialistically valid but it is important to ask whether it fulfil Habermas' criterion for legitimacy. In order to consider this question of legitimacy it is important to return to the grounded empirical study.

If we were to adapt s172 to include my suggestions of wider locus standi and enhance reporting obligations this would increase the scope of the law and consequently the liabilities of the directors. Consequently I think that the legitimacy of the amended provision would be hindered by both the complexity of the decisions facing directors and the continued ambiguity of how to rank the factors.

### **7.2.1 COMPLEXITY OF DECISIONS**

In the fashion retailing industry directors have to make judgements on a huge range of disputed issues. Taking two examples that arose from my research: plastic bags and waste stock, we can begin to see the complexity they face.

#### ***Plastic Bags.***

Two of my interviewees brought up the issue of plastic bags. At first I thought this gave a worrying indication of the level of sustainability understanding in the industry, I then realised it gives a ideal example of the complexity facing directors in UKFR. On the one hand the directors realised that plastic bags were bad for the environment and that Government will probably eventually implement legislation to control polybag use. On

the other hand, they were aware that paper-bags and other alternatives might have a higher albeit different environmental impact (and they are more expensive). Additionally their customers continue to demand plastic bags, so to stop using the bags would not only perhaps affect their profits, but also would have negligible environmental consequences. One way round this might be to charge for bags and place the onus on the customer to make the decision, but this option is not available for all business dilemmas; for example what to do with unsold stock.

### *Unsold Stock*

Two of my companies discussed very different management strategies for dealing with excess stock. One chose to sell clothes at cheaper and cheaper prices until all items were sold: passing the decision of waste management on to the customer, but adopting an approach which is open to criticism of promotion of impulse buying. Another chose to send their excess stock to an orphanage in Africa, who then sold it on the local market: certainly a philanthropic approach but also one that is not immune from reproach<sup>30</sup>. Other widely used waste disposal approaches include landfill and incineration, neither of which rate highly on environmental considerations<sup>31</sup>.

It could be argued that companies should just reduce the volume of stock they sell, however, high-street fashion is subject to short-term change: unseasonably warm weather, a VAT increase or even just an unpopular style can have major consequences for stock waste (Jackson & Shaw, 2008). For the time being there will inevitably be some unsold stock and directors must make decisions on how to deal with it.

This complexity has implications for the legitimacy of the law. Habermas maintains that *'institutionalised decision making loses contact with an uncoerced process of need articulation'* (1996: 427). He thinks that laws which encourage decision-making to be undertaken by a small number of people from one body, is illegitimate, even if these powers of deliberation have been delegated by democratic means, as the consequence would undermine the process of democracy. Moreover we should consider the consequences of assigning these societal decisions to those who are ultimately agents of the System (Mortimer, 2009).

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<sup>30</sup> Some claim that our apparel-waste floods the markets of developing countries, hindering local textile businesses (Baden & Barber, 2005).

<sup>31</sup> A detailed report has been produced which analyses textile waste in the UK (Morley et al, 2009). As well as illustrating the complexity of the issue, the report itself notes that the industry needs a commonly accepted standard (p119)



### 7.2.2 AMBIGUITY OF 'SUCCESS'

In society, the definition of sustainability is still unclear and so it is easier for us to pass the responsibility of sustainable management onto company directors. When we are unsure of our goal or the means in which to reach it, we inevitably resort to legislation which emphasises effective management (see **Box 3** p49). Directors already feel overburdened by their legislative responsibilities; from my interviews, I think it is unlikely that directors would accept even more onerous obligations for decision-making on them personally.

Additionally directors seems well aware of their responsibilities to consider multiple stakeholders and yet *'even the most socially concerned corporate and business managers find it difficult to simultaneously meet social, environmental and financial goals'* (Epstein, 2008:249). The current system of corporate governance in the UK is designed to maximise profit (Ward, 2008). S172 also falls within this paradigm view of the purpose of business: companies are considered successful if they have good economic growth.

**Box 3: Reasons for Choice of Regulation**

		Understanding of Regulatory Objective	
		High	Low
Understanding of Means	High	Command & Control	Information Based/Technology Based
	Low	Market/Performance Based	Management Based

Adapted from Hess, 2006 p 174

None of my interviewees would disagree that their companies require a healthy bottom-line, however, my interpretation is that this fails to fully grasp the purpose that they appear to have in their jobs. For example Interviewee A said *"I probably go out of my way to personalise the business... That's because I've grown up with it being a family business and a family ethos"* and Interviewee E said his concept of sustainability *'was more of a moral*

*compass... a view to what is right and wrong in what we are doing*'. This is not a unique finding; other studies found normative considerations are a key contributor to regulatory compliance (Gunningham et al, 2005:310).

All directors are required to make trade-offs and if we widen the scope of locus standi, it might make it more difficult still for executives to reach decisions that go against the immediate and determinate financial goals that are the presumption in our current definition of a successful company. The definition of success of a company is not limited to financial success, although it is the assumed goal (Hansard, 2006b). This might particularly be the case where the company is a public limited companies (PLC). In PLCs investors are protected from incurring huge liabilities which it could be suggested cultivates a culture of 'voluntary risk takers' and 'involuntary risk bearers' (Asmal, 2004:192).

It is unlikely that directors would view an increase in their personal liabilities as a legitimate response to reducing the effects of our lifestyles on the planet: especially in a consumer driven industry like fashion where the onus of ethical choices is still largely placed upon individual consumers. Two of my interviewees stated that they did not take part in the political process because they felt that their voices would not be heard. Habermas says that legitimacy comes when citizens recognise that they have had a role to play in creation of the law. If directors already feel disenfranchised and overburdened, it is unlikely that increasing their responsibilities will enhance their respect for the law.

### **7.3 LEGITIMACY AND COMPLIANCE**

The solutions that I suggest might in theory produce more positive environmental consequences for business, but in practice it is likely that directors will see themselves as unjustly overburdened undermining the legitimacy of the law. If the directors deem s172 as lacking in legitimacy then they are unlikely to act within the spirit of the law and may chose to report those risks that are least likely to see negative personal repercussions (Copp, 2009). Similarly they may choose to prioritise social factors over environmental concerns (as the environment has no title to sue). Finally it seems very unlikely that in this confusion directors would ever act in a way that would reduce their production and waste, if this meant reducing the companies profit. To act against the goal of profit maximisation no matter what their own moral leanings would probably be the most financially risky option for them personally. From the perspective of UKFR it seems that the lack of legitimacy which might surround the proposed amendments to s172 would seriously undermine its effectiveness.

### 8.1 CAN s172 OF THE UK COMPANIES ACT 2006 SUSTAINABLE THINKING IN THE BUSINESS DECISIONS OF COMPANY DIRECTORS?

The lack of awareness of s172 in my interviewees makes it difficult to reach a concrete answer to this question and I am reluctant to conclude that s172 has no effect. I would suggest that from my research s172 could promote sustainable decision-making in business but only in very specific circumstances: for example when shareholders' definition of the success of the company goes beyond that of short-term financial results.

This is arguably less likely in PLCs and larger companies where shareholders are more distant from the running of the business. Smaller companies, especially those with owner/directors seem more likely to adopt long-term visions for the company which are based less on economic results as the only gauge of success. However, in the fashion industry, the decisions of these directors are constrained by the 'race-to-the bottom' scenario which is fuelled by the 'stack them high, sell them cheap' mentality prevalent in today's market.

Where directors are taking long-term approaches to business decisions, it is highly likely that this is a result of diligent business practices rather than the threat of s172. One of the ways to make this easier to evaluate would be to inform directors of their duties under s172.

### 8.2 GUIDANCE FOR DIRECTORS

The law currently leaves the extent and content of the consideration of the factors under s172 to the individual discretion of the directors. Whilst this gives flexibility to companies, it also brings with it the danger of inconsistent and ineffective environmental management.

I asked my interviewees what was their interpretation of the concept sustainability. I obtained a plethora of responses: as Interviewee B put it *'it's a bit like religion, it is different*

*for different people*'. This makes it difficult to consider how a court would evaluate whether factors had been sufficiently considered.

Many companies (both within and outwith the fashion industry) have adopted voluntary codes of conduct as a means of self-regulation. These vary from company to company, especially in relation to environmental management. It is debateable whether guidelines must be made legally binding. If a regulatory body is endorsed by Government, courts may be more willing to interpret such a code as minimum standard required of a director. Voluntary adoption of codes can provide flexibility and be more effect (Wood, 2006). However they also lack the clarity, consistency and legitimacy of a recognised and universal third party code of practice (ibid).

Conversely, adherence to competition law rules is actively promoted in the UK and the Office of Fair Trading is known for its comprehensive regulatory stance (Worthington & Britton, 2006:413). Interviewee C suggested that his bosses took competition law extremely seriously. Business needs a body that promotes this level of concern in relation to environmental management.

In my opinion the UKFR needs a 'go-to' body for concise, trusted and readily available information. The DEFRA Roadmap might be a start; the recent conference bringing together more participants than ever before. On the other hand, the Roadmap currently suggests a cacophony of best practice ideas but lacks detailed guidance. Additionally only two of my interviewees were aware it existed (Interviewees C & D). Having now transferred its responsibility to WRAP (the organisation in charge of waste) it remains to be seen whether its profile will continue to rise. Even if it does become more widely considered, one criticism of the Roadmap is that many of its participants are larger firms which might lead some to doubt its transparency. Habermas notes that participation by companies in the public sphere can reinforce the colonisation of the Lifeworld and independent regulatory bodies are often criticised for working too closely with big business (Wood 2006:236).

In my interview with DEFRA, I was advised that *'there is a desire to raise the profile of sustainability.... and increase participation in the Roadmap'* with both business and consumers. Similarly they have not ruled out instigating universally applicable standards for the fashion industry; discussions in this area are on-going. It may be that in time the Roadmap leads to at least a clarification of the standards required of directors in UKFR.

### **8.3 THE EFFECT OF LONG-TERM THINKING**

Providing reliable guidelines for directors may not be enough. I found that director attitudes are not particularly the barriers to more sustainable business practices and that real power lies with the shareholders of industry heavyweights. In theory ESV should provide shareholders with the information they need to fully understand the consequences of profit making in the company, but in practice directors will only report on those environmental and social impacts that are likely to have a negative economic effect. Consequently long-term thinking will not work without additional regulations and consumer awareness.

The consequences of risk reporting on shareholder demand for short-term profits was outwith the scope of this thesis: however, it would offer further insight into how effective ESV is in practice. It would be interesting to investigate how many shareholders actually read the Business Reviews. Beyond this idea, many investments are held by other companies and hedge funds: further research could offer insight into how many people actually realise they are profiting from environmentally damaging practices in the fashion industry.

Without the demand for more ethical investments there really is little scope for long-term thinking to develop sustainable business models in the near future. In the fashion industry the short-term demands are so high and the market so volatile I do not think directors of companies will have time to envisage or create the kind of wide ranging closed-loop system that the business really needs to become sustainable. So whilst on an ad hoc basis companies might make improvements to linear models of production, at least within the fashion industry, the closed-loop approach is still a niche area.

### **8.4 LAW, BUSINESS AND THE REDUCTION OF CONSUMPTION**

Of course closing the loop is not the only approach to sustainable business; reducing our patterns of consumption would also have positive consequences for the environment. Nothing in my research suggests that business can be made to actively reduce our consumption by legal means. Businesses will continue to grow as long as we let them. A lot of research has been done on how businesses drive our levels of consumption: less time has been spent looking at how we as individuals drive business with our goals of financial success.

I think the shareholders of major corporations play a key, but as yet, under considered role in the sustainable consumption debate. In that sense my findings have lead me full circle, consumption is a collective responsibility and we all must consider our individual responsibilities within that collective.

## **8.5 HABERMAS AND LAW.**

Habermas advocates that law can stop the colonisation of the Lifeworld by the System, however, from a sustainability perspective this approach appears to be failing. I think this is because we have failed to recognise the extent to which the Lifeworld has already been colonised and the role law has played in that colonisation. Our corporate laws have seen companies personified and given the rights and, to a lesser extent, the responsibilities of a citizen. This has given companies a voice in the Lifeworld to the point that we now organise our institutions and laws for the maximisation of profit.

So effective has this colonisation been that we now see ourselves as victims of the structure and not agents in its creation. From my research I have no doubt that the directors in the fashion industry are limited by the structure of our corporate laws which constrain them in a business model that promotes unsustainable production. We also see that society is somewhat defenceless against the propagation of this idea of the value of material consumption. What appears to be less widely appreciated is that we are also driving this business model with our desire for financial returns on our investments.

I think that Habermas was right that law can limit the effects of colonisation, but it is probably necessary to expand his criteria for the creation public institutions to corporate entities. It appears that our environmental laws are battling -and often losing against- those laws which are designed to maximise production and profit. The market is designed to make money and so we need to make sure our laws make this as transparent and accountable as possible and in this sense corporate law fails. It largely promotes the short-term interests of the market. From a Habermasian perspective our corporate laws should not undermine the democratic process from which they were implemented, and at the moment it appears that they fall under the description 'legally sanctioned colonization' (Staats, 2004: 592)

## 8.6 THE FUTURE FOR LAW AND SUSTAINABLE DEVELOPMENT

To continue to advance sustainable development we must undertake a systematic review of corporate law<sup>32</sup>. Sustainability research should consider the ways in which corporate law hinders the criteria necessary for enlightened and informed decision-making and should evaluate and offer alternatives to those laws which seek only to maximise financial gains. Sound economics are necessary for, and an indicator of, a healthy company but in a sustainable society successful companies have to become more than just financially secure.

The Provision attempts to encourage sustainable thinking by financially penalising directors. Nothing from my research suggests that directors require a law to encourage them to give wider consideration to their business decisions. Nevertheless, in the fashion industry further dissemination of environmental and social effects is required. So long as some in the industry are allowed to accumulate capital without consideration of risk however, the companies can never really address the effects of their business. As Paul Hawken is quoted as saying *'we are faced with the sobering irony: if every company of the planet were to adopt the environmental and social practices of the best companies, the world would still be leading toward environmental collapse'*. (Elkington, 1997:38).

We need to approach business from a new angle and encourage personal responsibility in how we accumulate capital. From a practical sense further research is required into which laws isolate people from the corporate structure: for example limited liability frameworks; complex company structures; and reporting requirements. Ultimately I think we have to ask ourselves bigger questions, such as can we allow stakeholders to invest in companies for financial interests alone?

I agree with those who think we require more empirical research on corporations: both on individual companies and in different sectors. Not all sectors perform in the same way (fashion gives a very acute example of short-termism) and by analysing the corporate structures of successful individual companies we can begin to map out a company law system that is compatible with sustainable development.

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<sup>32</sup> In this thesis I have only studied the UK, however, such evaluation should occur on both a national and global level, to take account of the fact that our national corporate laws are locked in competition with those of other jurisdictions (Deakin, 2009).

## CONCLUSION

Current patterns of consumption are unsustainable. Despite attempts to encourage sustainable practices from individuals, our consumption levels continue to rise. Habermas argues that the System encourages material production and consumption and that law can limit the effect of this system on the Lifeworld. I agree with Habermas in that law can limit the influence of the System, however, my research has shown that it can also perpetuate the problem.

I found that by focusing on shareholders interests, the Provision limits the scope of sustainable thinking. Whilst certain amendments might, on paper, improve the effectiveness of the legislation, they will in practice have limited consequence for compliance with the Provision. This is because my proposed amendments of widening locus standi and reporting obligations also increase the complexity and ambiguity of directors' decisions, and thus in a Habermasian sense- reduce the legitimacy of the law.

S172 ultimately does little to provide sustainable thinking in business and we should not view its incorporation into corporate law as the completed project. Further research is required which analyses our current national and global corporate legislation to ensure that values contained within, go beyond financial consideration and are compatible with sustainable development. A comprehensive evaluation of corporate laws will provide further insight into how business can play a key role in sustainability.



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## APPENDIX 1: INTERVIEW QUESTIONS

1. **Directors role within the company**
  1. What are your responsibilities within the company?
  2. To whom (if anyone) do you feel you owe a duty of care to in undertaking your work?
  3. Where does this duty come from? (if prompting required suggest loyalty; contract; legal requirement; society morals)
  4. What tends to be your priority when making decisions for a) the company? b) in your personal life?
  5. Do you ever find that you are required to take decisions that you are uncomfortable with?
  6. What forces/prevents you from taking these decisions (for example time/money/regulations)
  
2. **Directors Opinion on the Nature and Importance of Sustainability.**
  1. Do you have a clear idea on the concept of sustainability? What does it entail?
  2. What has shaped your conceptualisation of the term sustainability?
  3. Do you think it is a universal term?
  4. Is the concept of sustainability important in your business? Why?
  5. Is it important to you as an individual? Why?
  6. (if prompting required suggest media, customers, conscience, law)
  7. Is the concept of sustainability more important in some areas of the business than others i.e. product design; supply chain sourcing; waste reduction; aftercare of products; labour rights?<sup>33</sup>
  8. Do you think adopting sustainability practices can:
    - a. Improve economic efficiency?
    - b. Strengthen your market position?
    - c. Improve your reputation in the media?
    - d. Reduce your liability under regulation?
    - e. Provide opportunities for growth?<sup>34</sup>
  9. Why?
  
3. **Directors knowledge of environmental concerns within the fashion industry**
  1. In your opinion is there a drive towards increased environmental consideration in fashion retailing?
  2. Where does this drive come from? What are the main concerns?
  3. Are you aware of any current schemes which promote environmental considerations within the fashion industry? (Give examples of DEFRA Roadmap: SMART Initiative: Centre For Sustainable Fashion )
  4. How do you keep up to date on developments in this area?
  5. Do you think the government will introduce future legislation which encourage environmental considerations within fashion retailing?
  6. In what form do you expect this legislation to take?
  7. Do you think it will affect your business? Positively? Negatively?
  8. Do you attempt to participate in policy making? If so, how? If not, why not?

### Final Question

Do you ever consider whether you or the company might, in future, be liable for failing to take into account environmental considerations in your decision making? Why?

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<sup>33</sup> This list is take directly from the Centre for Sustainable Fashion survey (2008) which looked at sustainability within the industry. I have taken their process because I presume they understand the important stages of the fashion retailing chain more than I do.

<sup>34</sup> This list corresponds largely with the research of the McKinsey report (2010).

## APPENDIX 2: INTERVIEWEE DATA

Interview	Company
A	Director - Small High Street Fashion Retailer
B	Director- Medium High Street Fashion Retailer
C	Sustainability Manager - Large High Street Fast Fashion Retailer
D	Director - Small Online Environmental Retailer
E	Director - Investment Company with a Number of High Street Brands

### APPENDIX 3: TABLE OF UKFR CSR REPORTING RESULTS

Company	CSR Policy on Website	Mentioned on Homepage	Environmental Info	Mention of Waste
A	X	X	X	X
B		X		
C		X		
D				
E	X	X	X	X
F		X		X
G	X	X	X	X
H	X	X	X	X
I		X		
J	X	X	X	X
K		X		
L				X
M				X
N	X	X	X	X
O	X	X		
P	X	X	X	X
Q	X	X	X	X
R	X	X	X	X
S			X	X
T	X	X	X	X
U				
V		X		
W		X	X	X
X*		X		
Y		X		
Z		X		X
AA	X	X	X	X
BB			X	X
CC	X	X	X	X
DD	X	X	X	X
EE	X	X	X	X
FF*		X		
GG	X		X	X
HH				X
II				X
JJ				
KK				
LL				
MM	X	X	X	X
NN*		X		X
OO	X	X	X	X
PP	X	X	X	X
QQ	X	X	X	X
RR				X
SS*				
TT*				

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**Table Key:**

Company Column

\* = PLC

Green = Eco-company

Information Columns

X = Information Missing

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**Total Statistics**

Companies with CSR policy  
online: 27/46

Companies with CSR policy on  
homepage: 15/46

Companies with Environmental  
Policy: 25/46

Companies with Waste Policy:  
17/46

**Section 214(4) of the 1986 Insolvency Act**

(4) For the purposes of subsections (2) and (3), the facts which a director of a company ought to know or ascertain, the conclusions which he ought to reach and the steps which he ought to take are those which would be known or ascertained, or reached or taken, by a reasonably diligent person having both

- a) the general knowledge, skill and experience that may reasonably be expected of a person carrying out the same functions as are carried out by that director in relation to the company, and
  - b) the general knowledge, skill and experience that that director has.
- 

**2006 Companies Act****s172: Duty to Promote the Success of the Company**

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

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has effect as if the reference to promoting the success of the company for the benefit of its members were to achieving those purposes.

3. The duty imposed by this section has effect subject to any enactment or rule of law requiring directors, in certain circumstances, to consider or act in the interests of creditors of the company.

**s174: Duty to Exercise Care, Skill and Diligence**

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.