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Social Responsibility Regulation and Its Challenges to Corporate Compliance

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SOCIAL RESPONSIBILITY REGULATION AND ITS CHALLENGES TO CORPORATE COMPLIANCE

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ABSTRACT

This Article addresses the intersection of corporate social responsibility and corporate compliance. In this context, the focus of this Article is on regulation that seeks to enhance socially responsible corporate conduct and its implications for the compliance function. Social responsibility regulation raises operational concerns for companies, including problems associated with assessing social performance, the proliferation and fragmentation of legal obligations, and the contested nature of the social issues that it addresses. As laws mandating socially responsible corporate conduct continue to grow in number and expand in scope, corporations will increasingly need to acknowledge and respond to these challenges.

INTRODUCTION

The growth of corporate compliance has been driven by the growing magnitude of the legal and regulatory requirements to which business is subject. Ensuring adherence to laws and regulation, as well as industry standards and internal policies, compels firms to look inward to determine how to most effectively deploy finite resources to compliance.[1] However, an excessively inward focus on the firm neglects another important actor: society and, by extension, the impact of the firm's compliance function on society.

To be sure, corporate compliance, as a field of study and an organizational function, includes awareness of corporate social responsibility (CSR).[2] Scholars of corporate compliance observe the inherent interrelationships between compliance and the firm's commitment

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1. *See* Robert C. Bird & Stephen Kim Park, *Turning Corporate Compliance into Competitive Advantage*, 19 U. PA. J. BUS. L. 285, 298 (2017) [hereinafter Bird & Park, *Turning Corporate Compliance*].

2. *See* GEOFFREY P. MILLER, THE LAW OF GOVERNANCE, RISK MANAGEMENT, AND COMPLIANCE 499 (2014) (characterizing CSR as an effort to "move corporations away from an exclusive focus on earning a profit for shareholders and more in the direction of providing value for society as a whole").

to ethical conduct, including CSR.[3] However, compliance and CSR are often characterized as distinct,[4] thus echoing broader normative and doctrinal debates in corporate law about the consideration of stakeholder interests in corporate governance.[5] There is a striking lack of consensus on whether social responsibility should be a part of the compliance function, with strongly-held views expressed by proponents and opponents alike.[6]

This Article posits that the question of whether compliance should address CSR is more and more a false choice. A small but growing number of regulatory mandates are emerging that impose obligations on companies to pursue, monitor, investigate, disclose, mitigate, or otherwise address CSR-related concerns and objectives for which they are deemed responsible, either through their own actions or the conduct of other actors with which they do business. Regulating social responsibility clarifies and strengthens the legal incentives for socially-beneficial corporate conduct.[7] In order to comply with these mandates, companies face the prospect of creating new internal governance mechanisms that are integrated into their respective compliance functions.[8] This emerging form of mandatory CSR, which this Article collectively refers to as social responsibility regulation, implicates the compliance function.[9]

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3. *See, e.g.*, Michele DeStefano, *Creating a Culture of Compliance: Why Departmentalization May Not Be the Answer*, 10 HASTINGS BUS. L.J. 71, 95 (2014) (observing that "the compliance function oversees not just what is legally required but also that which the corporation has set as the ethical obligations and social responsibilities of the corporation").

4. *See* Miriam A. Cherry, *The Law and Economics of Corporate Social Responsibility and Greenwashing*, 14 U.C. DAVIS L. & BUS. J. 281, 287–88 (2014) (referring to "bolted on" versus "baked in" CSR).

5. *See* Larry E. Ribstein, *Accountability and Responsibility in Corporate Governance*, 81 NOTRE DAME L. REV. 1431 (2006); Sean J. Griffith, *Corporate Governance in an Era of Compliance*, 57 WM. & MARY L. REV. 2075, 2123–25 (2016) [hereinafter Griffith, *Era of Compliance*].

6. *Compare* INT'L TRADE ADMIN., U.S. DEP'T OF COM., BUSINESS ETHICS: A MANUAL FOR MANAGING A RESPONSIBLE BUSINESS ENTERPRISE IN EMERGING MARKET ECONOMIES (2004), https://www.trade.gov/publications/pdfs/04BusinessEthics.pdf (incorporating CSR as an integral component of responsible business conduct), *with* Roy Snell, *Compliance Programs vs. Social Responsibility*, COMPLIANCE & ETHICS PROF., Sept. 2018, at 5, https://assets.corporatecompliance.org/Portals/1/PDF/Resources/Compliance_Ethics_Professional/0918/scce-cep-2018-09-snell.pdf (arguing that working on social issues detracts from compliance officers' core role of preventing and finding wrongdoing).

7. *See* Daniel T. Ostas, *Cooperate, Comply, or Evade? A Corporate Executive's Social Responsibilities with Regard to Law*, 41 AM. BUS. L.J. 559, 593 (2004) (arguing that "when comparing the relative potency of the letter of the law, the spirit of the law, and the desire to maximize profits, the letter of the law plays the smallest role" in determining how a firm will behave).

8. *See* Griffith, *Era of Compliance*, *supra* note 5, at 2124–25.

9. This Article addresses just a part of a growing universe of CSR manifested as law. Beyond the scope of this Article are several distinct forms of legally-enforceable CSR. Mandatory constituency statutes require corporations to consider stakeholder interests and, in some cases, grant enforcement rights to stakeholders. The most prominent example is the public benefit corporation statute. *See* J. Haskell Murray, *Adopting Stakeholder Advisory Boards*, 54 AM. BUS. L.J. 61, 81–83 (2017). In addition, this Article does not address various measures that firms

This Article explores this intersection of compliance and CSR by mapping out, in broad terms, the most prominent and influential examples of social responsibility regulation. These laws, independently enacted in numerous jurisdictions, promote a variety of social values, including, but not limited to, human trafficking, forced labor, climate change, and workers' rights.[10] Particularly in light of their ongoing proliferation, there is value in distilling the objectives and approaches of these laws.

As this Article shows, social responsibility regulation is distinct from other sources of regulatory and legal risk. The distinctive features of social responsibility regulation add a new layer of operational challenges to the compliance function.[11] This Article highlights three challenges. First, companies may find it difficult to assess compliance with social responsibility regulation. Second, social responsibility regulation features multiple sources of legal authority that define compliance in distinct ways and enforce CSR commitments through different means. Third and finally, social responsibility regulation underscores the importance of organizational culture to compliance. The very nature of the social issues subject to social responsibility regulation may trigger ambivalence, skepticism, or hostility among individual employees and senior management, which in turn hinders compliance efforts at the firm level.

To address these issues, this Article is organized as follows. Part I provides an overview of social responsibility regulation. The sources, content, procedures, and objectives of these regulatory mandates reveal the broad scope of this emerging area of corporate compliance. Part II examines the compliance-related challenges facing companies in respect of social responsibility regulation. Part III concludes with the implications of this Article's observations for the future of corporate compliance and social responsibility regulation.

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voluntarily undertake in order to act in a more socially responsible manner, such environmental-social-governance (ESG) investing and impact investing. *See* Beth Haddock, Tucker Pribor & Kate Starr, *Why Corporate Attorneys and Other Gatekeepers Should Consider ESG and Sustainability Principles*, 30 FORDHAM ENVTL. L. REV. 1 (2018). Nor does this Article directly address the compliance-related issues arising from shareholder proposals, which is increasingly being used by institutional investors to advance social issues such as gender diversity and equity, gun control, and climate change. *See* Robert C. Bird & Stephen Kim Park, *Organic Corporate Governance*, 59 B.C. L. REV. 21, 38–41 (2018); *see also* Scott Hirst, *Social Responsibility Resolutions*, 43 J. CORP. L. 217 (2018) (analyzing voting by institutional investors on social responsibility resolutions).

10. *See* MILLER, *supra* note 2, at 499 (describing social responsibility as "something of a grab bag").

11. *See* Veronica Root, *The Compliance Process*, 94 IND. L.J. 203, 209–10 (2019) (noting the breadth and diversity of issues for which compliance programs are responsible).

I. THE EMERGENCE OF SOCIAL RESPONSIBILITY REGULATION

The laws that constitute the small but expanding universe of social responsibility regulation are diverse in purpose and address a variety of social issues. They are implemented and enforced by governments in numerous jurisdictions at various levels. They are applied to business entities in different ways and with varying levels of specificity.

On a general level, the genus of social responsibility regulation is best classified by the mode of the regulatory mandate, which influences the nature and magnitude of the compliance risk faced by companies. The following discussion describes two primary archetypes of social responsibility regulation: (1) substantive regulation that mandates corporate conduct affecting society and (2) process-oriented requirements on corporate conduct, such as disclosure and due diligence.[12]

A. SUBSTANTIVE SOCIAL RESPONSIBILITY REGULATION

The first genus of social responsibility regulation consists of laws that impose broad-based CSR requirements of a substantive nature. Mandatory social regulation is arguably an oxymoron. Under a conception of CSR prevalent in the United States, the responsibility of a corporation to address the needs and demands of society is voluntary.[13] Therefore, corporate conduct defined in terms of CSR is essentially self-regulatory.[14] However, this voluntarist view is limited to the extent that CSR is perceived to be in conflict with the maximization of shareholder value.[15] As a counterpoint, various forms of state-centric CSR have emerged to address the perceived weaknesses of voluntarism.[16]

12. The examples identified and addressed below provide a representative overview of laws of greatest significance to multinational corporations rather than a comprehensive catalogue of social responsibility regulation worldwide.

13. Virginia Harper Ho, *Beyond Regulation: A Comparative Look at State-Centric Corporate Social Responsibility & the Law in China,* 46 VAND. J. TRANSNAT'L L. 375, 383 (2013) [hereinafter Harper Ho, *Beyond Regulation*] (referring to the common conception of CSR as "beyond regulation").

14. Afra Afsharipour & Shruti Rana, *The Emergence of New Corporate Social Responsibility Regimes in China and India*, 14 U.C. DAVIS BUS. L.J. 175, 179–80 (2013).

15. *See* Gerlinde Berger-Walliser & Inara Scott, *Redefining Corporate Social Responsibility in an Era of Globalization and Regulatory Hardening*, 55 AM. BUS. L.J. 167, 190–92 (2018) (critiquing voluntarism); *see also* Stefan J. Padfield, *Corporate Social Responsibility & Concession Theory*, 6 WM. & MARY BUS. L. REV. 1, 11 (2015) (identifying shareholder wealth maximization as the unifying theme of director primacy and shareholder primacy theories of corporate governance).

16. *See, e.g.*, Harper Ho, *Beyond Regulation*, *supra* note 13, at 391–95 (analyzing the European Union's relational-based CSR and contrasting it to the United States' market-based, self-regulatory approach); Afsharipour & Rana, *supra* note 14, at 227–29 (contrasting CSR laws in China and India with Western CSR models). State-centric CSR can also be non-regulatory, such as stakeholder constituency statutes. *See* Padfield, *supra* note 15, at 17–18.

Social responsibility regulation is most evident on its face in laws that mandate specific substantive obligations.[17] The most prominent examples are CSR mandates enacted by China and India that are incorporated into national laws governing the formation and operation of companies. The 2006 revision to China's Company Law requires that companies comply with social morality and undertake social responsibility.[18] In India, the Companies Act of 2013 imposes CSR requirements on companies among which include a minimum contribution of two percent of a company's average net profits to self-designated CSR activities.[19]

A variant of substantive social regulation is evident in France's Duty of Vigilance Law enacted in 2017.[20] Under this law, companies have an affirmative obligation of vigilance (*devoir de vigilance*)—that is, they must implement internal due diligence measures to identify and prevent human rights violations and environmental harm that could foreseeably arise in connection with their operations.[21] This due diligence obligation constitutes a duty of care for which a company may be subject to civil liability towards victims of either its own conduct or that of affiliates.[22] This law covers both French and foreign companies, and it applies to a company's supply chain relationships with subsidiaries and unaffiliated third parties.[23] Switzerland is currently debating proposals to enact legislation along similar lines.[24]

B. PROCESS-ORIENTED SOCIAL RESPONSIBILITY REGULATION

The second genus of social responsibility regulation consists of a range of regulatory strategies that seek to influence how companies address their

17. Berger-Walliser & Scott, *supra* note 15, at 205–06.

18. Company Law of the People's Republic of China (promulgated by the Standing Comm. Nat'l People's Cong., July 1, 1994, effective Jan. 1, 2006; rev'd Oct. 27, 2005), art. 5; *see also* Li-Wen Lin, *Corporate Social Responsibility in China: Window Dressing or Structural Change?*, 28 BERKELEY J. INT'L L. 64, 65 (2010) (referencing this provision of the Company Law).

19. The Companies Act, No. 18 of 2013, INDIA CODE (2013), § 135, http://www.mca.gov.in/Ministry/pdf/CompaniesAct2013.pdf; *see also* Afsharipour & Rana, *supra* note 14, at 217–19 (describing section 135 of the Companies Act).

20. *See* Loi 2017-399 du 27 mars 2017 relative au devoir de vigilance des sociétés mères et des entreprises donneuses d'ordre [Law 2017-399 of March 27, 2017 Relating to the Duty of Care of Parent Companies and Contractors], JOURNAL OFFICIEL DE LA RÉPUBLIQUE FRANÇAISE [J.O.] [OFFICIAL GAZETTE OF FRANCE], Mar. 28, 2017, https://www.legifrance.gouv.fr/eli/loi/2017/3/27/ECFX1509096L/jo/texte.

21. Sandra Cossart, Jérôme Chaplier & Tiphaine Beau de Lomenie, *The French Law on Duty of Care: A Historic Step Towards Making Globalization Work for All*, 2 BUS. & HUM. RTS. J. 317, 318–19 (2017).

22. *See* Dalia Palombo, *The Duty of Care of the Parent Company: A Comparison between French Law, UK Precedents and the Swiss Proposals*, 4 BUS. & HUM. RTS. J. 265, 276 (2019) (referencing Article 5 of France's Duty of Vigilance law).

23. Covered companies include any company incorporated or registered in France that employs at least 5,000 people (including through its French subsidiaries) or any foreign company that employs at least 10,000 people (including through subsidiaries located in France and abroad). Cossart et al., *supra* note 21, at 320.

24. *See* Palombo, *supra* note 22, at 276–78.

social and environmental impacts. The distinction between substantive social regulation and process-oriented social regulation lies in the relationship between the act of compliance and the desired regulatory outcome. In contrast to substantive social regulation, process-oriented social regulation does not mandate specific socially-beneficial conduct. Rather, these laws require the corporation to take actions based on the occurrence of certain events or conditions.[25] While the regulatory mandate to which the corporation must comply is essentially procedural, the underlying social policy objective is evident in the law itself.

The predominant mode of process-oriented social regulation in the United States is mandatory disclosure. Disclosure, as a regulatory technique, abounds in U.S. law.[26] In the vast universe of disclosure mandates are a growing number of laws requiring companies to disclose information regarding their non-economic social conduct and the impact thereof.[27] Disclosure requirements constitute a form of informational regulation, which uses the disclosure of firm-specific information as a means to influence market decisions by consumers and producers.[28] For example, customers of a polluting firm that become aware of the firm's conduct may engage in boycotting, litigation, lobbying, or protesting.[29]

The European Union's (EU) Directive on the Disclosure of Non-Financial Information was enacted in 2014.[30] The EU Non-Financial Disclosure Directive, which applies to corporations with 500 or more employees, specifically articulates the pursuit of CSR through mandatory corporate reporting as a guiding principle for its formulation.[31] Companies

25. *See* Bird & Park, *Turning Corporate Compliance*, *supra* note 1, at 319–20 (defining market contingent regulation); *see also* Margaret Ryznar & Karen E. Woody, *A Framework on Mandating Versus Incentivizing Corporate Social Responsibility*, 98 MARQ. L. REV. 1667, 1674–76, 1679–80 (2015) (describing how mandatory disclosure laws seek to influence corporate behavior through market pressure).

26. Omri Ben-Shahar & Carl E. Schneider, *The Failure of Mandated Disclosure*, 159 U. PA. L. REV. 647, 652–65 (2011) (describing several paradigmatic examples).

27. *See* Stephen Kim Park, *Targeted Social Transparency as Global Corporate Strategy*, 35 NW. J. INT'L L. & BUS. 87, 94 (2014) [hereinafter Park, *Targeted Social Transparency*]; *see also* David Hess, *The Transparency Trap: Non-Financial Disclosure and the Responsibility of Business to Respect Human Rights*, 56 AM. BUS. L.J. 5, 19–26 (2019) (describing mandatory non-financial disclosure regimes that address human rights).

28. Sarah E. Light & Eric W. Orts, *Parallels in Public and Private Environmental Governance*, 5 MICH. J. ENVTL. & ADMIN. L. 1, 39 (2015).

29. *Id.* at 40.

30. *See* Council Directive 2014/95, of the European Parliament and of the Council of 22 October 2014 Amending Directive 2013/34/EU as Regards Disclosure of Non-Financial and Diversity Information by Certain Large Undertakings and Groups, 2014 O.J. (L 330).

31. *See id.* at 1 ("[T]he European Parliament called on the Commission to bring forward a proposal . . . in order to take account of the multidimensional nature of corporate social responsibility (CSR) and the diversity of the CSR policies implemented by businesses matched by a sufficient level of comparability to meet the needs of investors and other stakeholders as well as the need to provide consumers with easy access to information on the impact of businesses on society.").

are required to provide disclosure on environmental matters, social and employee-related matters, respect for human rights, and anti-corruption and bribery matters in their annual reports on a comply-or-explain basis.[32]

In contrast to the EU, the Securities Exchange Commission (SEC) has been relatively disengaged on mandatory social disclosure. In its 2010 guidance on the materiality of climate change-related risk, the SEC identified specific areas in which disclosure under federal securities law would be required by reporting companies.[33] More recently, the SEC has solicited public comment on amendments to Regulation S-K, including emerging risks such as ones associated with issuers' environmental and social impacts and practices.[34] However, the SEC's 2016 Concept Release has not subsequently led to steps towards the implementation of mandatory reporting of social and other non-financial risks.[35]

Rather than general mandates, the use of disclosure to regulate social responsibility in the United States is characterized by specialized disclosure frameworks and private standards.[36] The SEC has adopted regulations pursuant to the Dodd-Frank Act that mandate disclosure of the use of conflict minerals in supply chains,[37] certain business activities in Iran,[38] and

32. In a comply-or-explain model, a company may comply with a regulation (such as a code of best practices) either by implementing the regulation's principles or providing an explanation for why it has elected not to follow them. Virginia Harper Ho, *"Comply or Explain" and the Future of Nonfinancial Reporting*, 21 LEWIS & CLARK L. REV. 317, 321 (2017).

33. Commission Guidance Regarding Disclosure Related to Climate Change, Securities Act Release No. 9106, Exchange Act Release No. 61,469, 97 SEC Docket 2414 (Feb. 2, 2010).

34. *See* Business and Financial Disclosure Required by Regulation S-K: Concept Release, Securities Act Release No. 10,064, Exchange Act Release No. 77,599, 81 Fed. Reg. 23,921, 23,956 (Apr. 22, 2016); *see also* Virginia Harper Ho, *Nonfinancial Risk Disclosure & the Costs of Private Ordering*, 55 AM. BUS. L.J. 407, 425–30 (2018) [hereinafter Harper Ho, *Nonfinancial Risk Disclosure*] (describing current rules and practices regarding disclosure of non-financial information).

35. One notable exception is the initial step by the SEC towards mandating "human capital" disclosures. *See* Modernization of Regulation S-K Items 101, 103, and 105, Securities Act Release No. 10,668, Exchange Act Release No. 86,614, 84 Fed. Reg. 44,358, 44, 369–72 (Aug. 23, 2019). That notwithstanding, SEC officials have expressed outright skepticism and hostility to ESG-based analysis in the securities markets. *See, e.g.*, Hester Peirce, Comm'r, Sec. & Exch. Comm'n, Scarlet Letters: Remarks before the American Enterprise Institute (June 18, 2019), https://www.sec.gov/news/speech/speech-peirce-061819 (criticizing proxy advisors, investment advisers, shareholder proponents, non-investor activists, as well as the EU and the International Organization of Securities Commissions, and likening their use of ESG criteria to assess corporations to Hester Prynne's scarlet letter).

36. Previously, I have collectively referred to disclosure laws that address geographically defined and/or issue-specific social policy objectives as "targeted social transparency." *See* Park, *Targeted Social Transparency*, *supra* note 27.

37. *See* Dodd–Frank Wall Street Reform and Consumer Protection Act of 2010, Pub. L. No. 111–203, § 1502, 124 Stat. 1376, 2213 (2010), codified at 15 U.S.C. § 78m (2012) [hereinafter Dodd-Frank Act]. In 2017, the EU enacted a comparable conflict minerals reporting regime, which will become effective in 2021. *See* Regulation (EU) 2017/821 of the European Parliament and of the Council of 17 May 2017, 2017 O.J. (L 130).

38. Iran Threat Reduction and Syria Human Rights Act of 2012, Pub. L. No. 112–158, § 219, 126 Stat. 1214, 1235–36.

mine safety.[39] In the absence of more robust guidance and regulation by the SEC, various private organizations have created disclosure frameworks of varying scope and objectives to assist companies in their voluntary disclosure of environmental, social, and governance (ESG) information.[40]

Process-oriented social regulation may combine mandatory disclosure of specific social issues with due diligence. The most notable examples of this regulatory approach worldwide have been enacted by the United Kingdom,[41] Australia,[42] and California.[43] These laws seek to combat modern slavery, forced labor, and human trafficking by requiring companies to disclose their voluntary efforts to identify and eliminate human rights violations.[44] For example, the California Transparency in Supply Chains Act requires companies to report on five aspects of their supply chain due diligence: verification, audits, certification, internal accountability, and training.[45] Under these laws, companies are not legally required to engage in due diligence. Instead, the act of disclosure itself constitutes compliance. A company's efforts to address the human rights issue is not subject to regulatory enforcement nor is it required to achieve a specific policy goal, such as the elimination of human rights violations.[46] Rather than mandating specific conduct, these laws aim to induce companies to undertake due diligence of their supply chains by equipping consumers, civil society activists, and other stakeholders with pertinent information regarding a given company's efforts.[47]

39. *See* Dodd-Frank Act § 1503, 124 Stat. 1376, 2218 (2010); 17 C.F.R. § 229.104 (2019) (mine safety); *see also* Mine Safety Disclosure, Securities Act Release No. 9164, Exchange Act Release No. 63,548, 76 Fed. Reg. 81,762 (Dec. 15, 2010).

40. Most notable among them are standards established by the Global Reporting Initiative (GRI), the Sustainability Accounting Standards Board (SASB), the International Integrated Reporting Council (IIRC), and the Climate Disclosure Project (CDP). *See* Ruth Jebe, *The Convergence of Financial and ESG Materiality: Taking Sustainability Mainstream*, 56 AM. BUS. L.J. 645, 661–65, 667–69 (2019).

41. *See* Modern Slavery Act 2015, c. 30 (UK).

42. *See* Modern Slavery Act 2018 (Cth) (Austl.).

43. *See* CAL. CIV. CODE § 1714.43 (Deering 2019) (the "California Transparency in Supply Chains Act") [hereinafter CTSCA].

44. Hess, *supra* note 27, at 45.

45. CIV. § 1714.43(c).

46. *See* Jena Martin, *Hiding in the Light: The Misuse of Disclosure to Advance the Business and Human Rights Agenda*, 56 COLUM. J. TRANSNAT'L L. 530, 569–70 (2018) (criticizing remedies available for non-compliance with disclosure and due diligence laws); Adam S. Chilton & Galit A. Sarfaty, *The Limitations of Supply Chain Disclosure Regimes*, 53 STAN. J. INT'L L. 1, 15–18 (2018) (analyzing compliance with CTSCA).

47. Chilton & Sarfaty, *supra* note 46, at 4.

II. THE COMPLIANCE CHALLENGES OF SOCIAL RESPONSIBILITY REGULATION

Corporate compliance can be understood as a process consisting of four distinct stages: prevention, detection, investigation, and remediation.[48] Social responsibility regulation—particularly the process-oriented social regulation most applicable to corporations based or operating in the United States—imposes pressures at the prevention and detection stages. The diversity of social responsibility regulation, evident in the examples described in Part I above, obscures common concerns.

The following discussion highlights and explores three challenges in particular: (1) the problem of measuring and assessing compliance across a corporation's operations, (2) the proliferation and consequent fragmentation of legal obligations and regulatory mandates to which corporations are subject, and (3) the role of individually-held moral values in the establishment of an organizational culture of compliance. These issues—while not unique to social responsibility regulation—nonetheless pose particularly significant challenges and, furthermore, raise provocative questions about the capacity of business to effectively carry out the policy goals underlying social responsibility regulation.

A. ASSESSMENT

A common criticism of social responsibility regulation is the cost of compliance due to the diversity of issues and operational activities for which the corporation must collect information or otherwise address.[49] Social responsibility regulation that addresses human rights and labor conditions typically focuses on the process by which a product was made.[50] For a multinational corporation with global supply chains, this involves monitoring and analyzing the conduct of subsidiaries, third-party suppliers, and contractors. The SEC's conflict minerals reporting regime has attracted vocal critics, who cite compliance costs as a key basis for their opposition.[51] The decentralized, organizationally heterogeneous structure of multinational corporations heightens this challenge due to the frequent separation of in-house substantive experts on social responsibility regulation (who may be in legal, compliance, or a standalone CSR or

48. *See* Root, *supra* note 11, at 220.

49. *See* Jeff Schwartz & Alexandra Nelson, *Cost-Benefit Analysis and the Conflict Minerals Rule*, 68 ADMIN. L. REV. 287, 300–18 (2016) (detailing the compliance costs analyzed by the SEC in its rulemaking on conflict minerals). Schwartz and Nelson criticize the SEC's quantification of compliance costs, concluding that actual compliance costs have been far less than the SEC's estimates. *See id.* at 327–29.

50. Chilton & Sarfaty, *supra* note 46, at 23–24.

51. *See* Galit A. Sarfaty, *Human Rights Meets Securities Regulation*, 54 VA. J. INT'L L. 97, 111–12 (2013) (referencing criticism from industry groups and the U.S. Chamber of Commerce).

sustainability function) and the operational units or subsidiaries responsible for implementing it.[52]

The debate about compliance costs is really a matter of the cost of compliance relative to its benefits, whether accruing to the firm itself or society generally. In that respect, social responsibility regulation is not hindered by a lack of metrics available to firms for measuring their own social performance.[53] Rather, the problem of assessment is due to a lack of consensus on how to measure and assess social performance, thus hindering the ability of firms to meaningfully comply. For example, under its conflict minerals reporting rules, the SEC mandates that companies using such minerals undertake supply chain due diligence under the Organization for Economic Cooperation and Development (OECD) Due Diligence Guidance for Responsible Supply Chains of Minerals from Conflict-Affected and High-Risk Areas.[54] However, due to the lack of prescriptive and comprehensive guidance, companies struggle to apply the OECD Due Diligence Guidance to specific countries and industries.[55]

This lack of consensus arguably unmoors compliance from its regulatory rationales.[56] Compliance with social responsibility regulation—like corporate compliance generally—is vulnerable to metrics and internal assessment that track what firms do (i.e., efforts) rather than what they actually accomplish (i.e., outcomes).[57] For example, disclosure regimes define materiality in different ways. This provides firms with significant discretion to determine what to disclose—with no universally recognized means to determine whether one company's definition aligns with its counterparts in the industry or market, or whether a company's definition of a material event or risk under one regulatory regime matches the definition

52. *See* Veronica Root, *Complex Compliance Investigations*, COLUM. L. REV. (forthcoming), (manuscript at 24–26), https://ssrn.com/abstract=3350463 (describing Walmart's organizational reforms to a global bribery scandal).

53. *See* Harper Ho, *Nonfinancial Risk Disclosure*, *supra* note 34, at 447.

54. Galit A. Sarfaty, *Shining Light on Global Supply Chains*, 56 HARV. INT'L L.J. 419, 438 (2015) [hereinafter Sarfaty, *Shining Light*].

55. *See id.* at 448–49; Jeff Schwartz, *The Conflict Minerals Experiment*, 6 HARV. BUS. L. REV. 129, 165 (2016) (noting the compliance challenges arising from companies' differing interpretations of the OECD's Due Diligence Guidance).

56. *See* Christine Parker, *The "Compliance" Trap: The Moral Message in Responsive Regulatory Enforcement*, 40 L. & SOC. REV. 591, 609 (2006) ("*Compliance* is meaningless, or rather has contested meanings, in the absence of some commonly accepted understanding of the way regulatory requirements should be interpreted and applied.").

57. *See* CASEY O'CONNOR & SARAH LABOWITZ, PUTTING THE "S" IN ESG: MEASURING HUMAN RIGHTS PERFORMANCE FOR INVESTORS 18–20 (2017) (noting the emphasis of voluntary social disclosure initiatives on efforts rather than effects), https://static1.squarespace.com/static/547df270e4b0ba184dfc490e/t/58cad912e58c6274180b58b6/1489688854754/Metrics-Report-final-1.pdf; *see also* Martin, *supra* note 46, at 577 (arguing that efforts-based social disclosure, such as conflict minerals reporting, is predominant due to the fact that it is easier for companies to measure); Griffith, *Era of Compliance*, *supra* note 5, at 2105 (critiquing the misguided use of metrics by the compliance function).

that it uses under any other. Most forms of social responsibility regulation lack direct regulatory oversight, thereby leading to wildly varying levels of compliance. Some companies comply beyond the law, while others comply with only the letter of the law (if not its spirit) or not at all.[58]

B. FRAGMENTATION

A second challenge to corporate compliance raised by social responsibility regulation is the sheer number, diversity, and geographic scope of legal and regulatory mandates. This source of compliance risk is particularly pertinent to multinational corporations that operate worldwide. Like many other areas in which companies have invested heavily in compliance, corporations face different substantive obligations and procedural requirements across multiple jurisdictions.[59]

Most notably, social responsibility regulation substantially involves compliance obligations of a private nature. Compliance obligations may be privatized in a couple of ways. First, voluntary private standards have emerged as an integral means of regulating the relationship between business and civil society through CSR.[60] These private governance regimes, established by firms or non-governmental organizations (NGOs), operate with varying levels of autonomy and collaboration vis-à-vis governmental regulation.[61] Second, private contracts and third-party codes of conduct increasingly reference CSR and related social commitments, such as human rights and sustainable development.[62] These references may be to social responsibility regulations, as described in Part I above, or to private CSR standards. In either case, these obligations are subject to

58. *See* Schwartz, *supra* note 55, at 166–67 (analyzing the first year compliance filings under the SEC's conflict minerals regulation); Chilton & Sarfaty, *supra* note 46, at 15–18 (analyzing disclosures under the California Transparency in Supply Chains Act).

59. *See* Jamie Darin Prenkert & Scott J. Shackelford, *Business, Human Rights, and the Promise of Polycentricity*, 47 VAND. J. TRANSNAT'L L. 451, 474–93 (2014) (cataloging the numerous governmental and non-state actors that regulate the use of conflict minerals).

60. *See* Cynthia A. Williams, *A Tale of Two Trajectories*, 75 FORDHAM L. REV. 1629, 1639–41 (2006); *see also* DAVID VOGEL, THE MARKET FOR VIRTUE: THE POTENTIAL AND LIMITS OF CORPORATE SOCIAL RESPONSIBILITY (2006).

61. *See* Kenneth W. Abbott & Duncan Snidal, *Strengthening International Regulation Through Transnational New Governance: Overcoming the Orchestration Deficit*, 42 VAND. J. TRANSNAT'L L. 501, 512–19 (2009) (including private and public-private standards in their analysis of transnational regulatory standard-setting); Martijn W. Scheltema, *Assessing Effectiveness of International Private Regulation in the CSR Arena*, 13 RICH. J. GLOBAL L. & BUS. 263, 272–73 (2014) (noting that public regulators may jointly develop rules with private actors or incorporate private standards into new or existing laws or regulations); Grainne de Búrca, Robert O. Keohane & Charles Sabel, *New Modes of Pluralist Global Governance*, 45 N.Y.U. J. INT'L L. & POL. 723, 733–38 (2013) (observing that governments participate in various networks and governance arrangements with companies, NGOs, and other non-state actors).

62. *See* Scott Killingsworth, *The Privatization of Compliance RAND Center for Corporate Ethics and Governance Symposium White Paper Series, Symposium on "Transforming Compliance: Emerging Paradigms for Boards, Management, Compliance Officers, and Government*" (2014), at 4–5, https://ssrn.com/abstract=2443887.

contractual enforcement by a firm's counterparties and thus within the scope of the compliance function.[63]

This regulatory environment—characterized by regulatory mandates and contractual commitments across a range of jurisdictions and established by government and non-state actors—creates fragmentation.[64] On a market or industry-wide level, fragmentation may increase uncertainty among market participants and lower levels of compliance.[65] For example, different definitions of materiality applied by private ESG disclosure frameworks can lead to incomplete and incomparable information being disclosed, thereby diminishing its usefulness to investors and stakeholders.[66] Further, on a firm-specific level, fragmentation may exacerbate the burden on compliance programs to track the firm's compliance risks.[67]

C. VALUES

A third challenge to corporate compliance is the potential conflict arising from the cultural or moral values associated with social responsibility regulation. The effectiveness of a compliance program hinges on aligning with the values of the company's employees.[68] If employees perceive a compliance mandate to be unintelligible and illegitimate, this may undermine the compliance mandate by leading employees to rationalize their unethical or illegal conduct.[69] If senior management acts in a way that is inconsistent with the policy goals of the regulatory mandate, then its perceived value will drop in the eyes of employees, who may decide to shirk their responsibility to comply.[70]

63. *Id.* at 33–34 (noting legal risk from potential indemnities, damages, audits, default declarations, and loan acceleration and termination).

64. In international law, fragmentation is defined as "conflicts between rules or rule-systems, deviating institutional practices and, possibly, the loss of an overall perspective on the law." Int'l Law Comm'n, Fragmentation of International Law: Difficulties Arising from the Diversification and Expansion of International Law, U.N. Doc. A/CN.4/L.682, at 11 (2006), as corrected U.N. Doc. A/CN.4/L.682/Corr.1 (2006).

65. Stephen Kim Park, *Investors as Regulators: Green Bonds and the Governance Challenges of the Sustainable Finance Revolution*, 54 STAN. J. INT'L L. 1, 36 (2018). In the absence of international regulation or some form of stakeholder-oriented oversight, fragmentation may also lead to a regulatory race-to-the-bottom as firms seek to avoid or minimize the cost of regulatory compliance. Stephen Kim Park & Gerlinde Berger-Walliser, *A Firm-Driven Approach to Global Governance and Sustainability*, 52 AM. BUS. L.J. 255, 289 (2015).

66. *See* Jebe, *supra* note 40, at 665.

67. *See* Killingsworth, *supra* note 62, at 10.

68. *See* Todd Haugh, *Nudging Corporate Compliance*, 54 AM. BUS. L.J. 683, 737–38 (2017); Sean J. Griffith, *The Question Concerning Technology in Compliance*, 11 BROOK. J. CORP. FIN. & COM. L. 25, 30 (2016) (citing Lynn Sharp Paine, *Managing for Organizational Integrity*, HARV. BUS. REV., Mar.–Apr. 1994).

69. Todd Haugh, *The Criminalization of Compliance*, 92 NOTRE DAME L. REV. 1215, 1217–18 (2017).

70. *See* David Hess, *A Business Ethics Perspective on Sarbanes-Oxley and the Organizational Sentencing Guidelines*, 105 MICH. L. REV. 1781, 1801 (2007).

Arguably, social responsibility regulation is particularly vulnerable to this problem due to deeply held personal views about the appropriate role of business in addressing societal needs or even about the validity of the social goals themselves. Most social responsibility regulation addressed in this Article employs relatively weak formal sanctions, instead relying on informal sanctions such as "naming-and-shaming."[71] Thus, in order for social responsibility regulation to be effective across different companies and industries, there must be a modicum of moral commitment by employees to its tenets.[72] Without it, compliance is at risk of being a simulacrum—a ritual without meaning. Companies may engage in greenwashing[73] or may comply with social regulation in a ritualistic, "check-the-box" manner.[74] To cite one prominent example, the Deepwater Horizon oil spill in 2010 revealed the pervasiveness of BP's safety compliance failures despite publicly touting its commitment to social responsibility.[75]

CONCLUSION

In the United States and elsewhere, the responsibility of corporations to society has sparked strong reactions from advocates and critics alike. Despite the commitments of corporations to social responsibility,[76] there is widely-held sentiment that regulation is necessary to hold corporations accountable.[77] Notwithstanding the ongoing debates about the merits of CSR or regulatory capture versus overreach, this Article seeks to contextualize social responsibility regulation within corporate compliance as a starting point for further engagement between legal scholars and compliance professionals.

A fertile area for future research arises from the need to foster social responsibility regulation that enables corporations to develop new patterns

71. *See* Schwartz, *supra* note 55, at 161–65 (highlighting the ineffectiveness of naming-and-shaming with conflict minerals disclosures).

72. *See* Parker, *supra* note 56, at 591–92, 610–11 (highlighting the need for moral commitment to ensure sustainable compliance).

73. Greenwashing includes "elements of deception, deployment of CSR as a distraction, and an element of hypocrisy." Cherry, *supra* note 4, at 285.

74. *See* Galit A. Sarfaty, *Regulating through Numbers: A Case Study of Corporate Sustainability Reporting*, 53 VA. J. INT'L L. 575, 606–07 (2013) (noting this risk in the context of a study of the GRI); *see also* Parker, *supra* note 56, at 611 (noting the possibility of regulatory capitulation to business preferences regarding interpretation and enforcement).

75. *See* Miriam A. Cherry & Judd F. Sneirson, *Beyond Profit: Rethinking Corporate Social Responsibility and Greenwashing After the BP Oil Disaster*, 85 TUL. L. REV. 983, 995–99, 1002–09 (2011).

76. *See Statement on the Purpose of a Corporation*, BUSINESS ROUNDTABLE (Aug. 19, 2019), https://opportunity.businessroundtable.org/wp-content/uploads/2019/09/BRT-Statement-on-the-Purpose-of-a-Corporation-with-Signatures-1.pdf.

77. *See, e.g.*, Cynthia A. Williams, *The Securities and Exchange Commission and Corporate Social Transparency*, 112 HARV. L. REV. 1197 (1999) (arguing for expanded social disclosure through SEC reporting requirements).

of decision making based on prior experiences with regulators and other external actors imposing legal mandates.[78] The ample literature on responsive regulation recognizes that regulatory compliance is most effective when it dynamically and flexibly leverages economic, social, and normative motives to comply.[79] In parallel, New Governance theory recognizes the value of regulatory learning in order to improve the application of policy through governance-based regulation.[80] The onus to facilitate organizational learning lies both with regulators and firms. Within existing rules or the establishment of new regulatory frameworks, regulators can more effectively engage with firms.[81] Likewise, corporations can take steps to improve their corporate culture so that social responsibility regulation becomes the domain of the entire organization instead of being confined to in-house counsel or the compliance function.[82] The long-term viability of CSR depends on the capacity of the corporate compliance function to meaningfully implement social responsibility regulation.

78. *See* Park, *Targeted Social Transparency*, *supra* note 27, at 113 (exploring how companies can learn through complying with mandatory disclosure requirements).

79. *See* Vibeke Lehmann Nielsen & Christine Parker, *Testing Responsive Regulation in Regulatory Enforcement*, 3 REG. & GOVERNANCE 376, 378–79 (2009) (citing IAN AYRES & JOHN BRAITHWAITE, RESPONSIVE REGULATION: TRANSCENDING THE DEREGULATION DEBATE (1992)); *see also* Vibeke Lehmann Nielsen & Christine Parker, *Mixed Motives: Economic, Social, and Normative Motivations in Business Compliance*, 34 L. & POL'Y 428, 431–33 (2012) (describing these motives to comply).

80. *See* Orly Lobel, *The Renew Deal: The Fall of Regulation and the Rise of Governance in Contemporary Legal Thought*, 89 MINN. L. REV. 342, 396–400 (2004).

81. *See, e.g.*, Kenneth A. Bamberger, *Regulation as Delegation: Private Firms, Decisionmaking, and Accountability in the Administrative State*, 56 DUKE L.J. 377, 458–67 (2006) (discussing the role of regulators as educators).

82. *See* Sarfaty, *Shining Light*, *supra* note 54, at 423.