Industry, academics weigh in on ethics, diversity, future of Dodd-Frank

By Amy Leisinger, J.D.

Social responsibility, board diversity, and ethical issues facing boards have become increasing pressing issues in corporate governance, according to panelists at a conference hosted by Loyola University School of Law’s Institute for Investor Protection. Shareholders expect more from companies than just growth and dividends, but increased focus on these issues and general corporate behavior could serve to achieve both social and financial goals simultaneously, they explained. Many related Dodd-Frank requirements remain up the air as the Trump Administration and Congress explore potential changes, but the panelists agreed that federal and state regulators will continue to step up efforts to support investor protection and boards can play an important role in the process.

Loyola’s own Seth Green noted that business are spending billions of dollars on corporate social responsibility activities, increasing participation in sustainable investments, and enhancing environmental, social, and governance criteria. According to Green, companies are embracing social good and going beyond compliance and typical corporate governance standards to meet societal expectations and employees’ desires to make an impact and create social value throughout their careers. By intertwining social responsibility with actual business activities and making long-term investments in addressing social and environmental concerns, corporations can create value and increase growth, particularly in light of increasing consumer interest in sustainability, he said.

Ultimately, companies exist for benefit shareholders, and boards may not want to incidentally benefit shareholders primarily to help others, he explained. However, the industry is seeing an increasing competitive advantage to “doing good,” and, arguably, long-term benefits accruing to shareholders far in the future can be justified under the business judgment rule, Green said. To support the feasibility of socially responsible business, some states have adopted Low-Profit Limited Liability Corporation (L3C) structures, a new kind of organization that combines the financial and liability advantages of a traditional LLC with the social benefits of a non-profit. These entities require a primary purpose to further charitable, educational, or social goals with financial gains as a secondary consideration, he explained.

Many take issue with the increasing corporate focus on social and ethical concerns by arguing that the companies must be run for the benefit of shareholders, but Loyola professor Steven Ramirez noted that management profits the most from corporate operations, not shareholders. Shareholders do not benefit from corporate misconduct,
and, during the financial crisis, the industry saw a breakdown in accountability, according to Ramirez. Ethical outcomes are material to shareholders, and corporations should disclose what the firm is doing, he said. Holding management accountable and requiring disclosure of ethical structures while acclimating to shareholder demands for socially and ethically sound activities would lead to market-based ethicality and enhanced performance, he opined.

The panelists concurred that boards have seen gains in diversity but noted that progress has stalled. Sometimes, diverse board members become tokenized and their opinions end up isolated, according to panelists. As such, they agreed that compliance needs to play a role and that the SEC should consider enhancements to its board diversity rules to require additional disclosures with regard to corporate diversity policies. Different backgrounds lead to different viewpoints, which will benefit shareholders—a very diverse group of individuals, they concluded.

Journalist and author Bethany McLean noted that, while it is crucial for shareholders and consumers to take personal responsibility for what they buy, companies also need to take responsibility for what they sell, and executives profiting from potentially unethical decisions should bear the risk. The panelists suggested that the most pressing consideration is the tone at the top and a focus not on what is written down in policies and procedures but instead on what is actually being done. Bob Chung, general counsel for Arete Wealth Management, suggested that the best way to get management to accept ethical ideals is to drive them to be mindful about ethical concerns. There is often confusion between compliance and ethics, he noted, and, ultimately, executives need to model behavior for both other executives and employees and encourage good choices. Corporate codes of ethics could help to create a positive culture, the panelists agreed.

In considering the future of the Dodd-Frank Act, panelists noted that it seems unlikely that all of the reforms will be rolled back. For example, Howard Suskin of Jenner & Block suggested that some protections will remain and new ones will evolve; state attorneys general are already jumping into consumer protection, even if entities like the Consumer Financial Protection Board lose authority, he said. Egregious fraud allegations will always transcend political lines, Suskin explained. University of Denver professor Celia Taylor agreed, noting that the conflict minerals rule has suffered blows and that the SEC chairman has said he will not enforce the remainder of the rule but companies are still reporting and learning more about supply chains, often in response to positive shareholder feedback.

The House passed the CHOICE Act to reform Dodd-Frank, but the legislation seems to have stalled, the panelists explained.

Former United States District Court Judge Shira Scheindlin closed the conference with remarks on Dodd-Frank, ethics, and diversity. In her 22-year tenure in the Southern District of New York, she noted, politics inevitably figured into the equation and will continue to play a role. The key will be retaining incentives to come forward to prevent and respond to fraud and other misconduct, she explained, and private enforcement and class actions will be crucial in response to Dodd-Frank changes. Businesses and shareholders need to encourage an internal desire to do the right thing, and, hopefully, private responsibility will move in to fill the gap as financial regulation evolves, according to Scheindlin. Indeed, she opined, it appears that as the government is stepping down on regulation, the private sector is stepping up.

Diversity is always a consideration, and study after study confirms that diversity leads to better decisions, she explained. While public organizations seem to be achieving diversity goals, the private sector lags behind, Scheindlin said, particularly in alternative dispute resolution, which she has firsthand in her current rule as an arbitrator and mediator. Companies must put effort into achieving diversity, but, in reality, this will require a substantial culture shift, Scheindlin concluded.