



ELSEVIER

Contents lists available at [ScienceDirect](#)

Critical Perspectives on Accounting

journal homepage: www.elsevier.com/locate/cpa



Full length article

Explanations for corporate governance non-compliance: A rhetorical analysis

Philip J. Shrides^{a,*}, Niamh M. Brennan^b

^aNewcastle Business School, Northumbria University, United Kingdom

^bUniversity College Dublin, Ireland

ARTICLE INFO

Article history:

Received 12 January 2016

Received in revised form 14 August 2017

Accepted 15 August 2017

Available online xxx

In memoriam: This paper is dedicated to the memory of Professor David J. Campbell 1963–2017, a great colleague and friend.

Keywords:

Corporate governance Code

Comply-or-explain

Non-compliance

Explanation

Rhetoric

Typology

ABSTRACT

A central element of many corporate governance codes is the 'comply-or-explain' system, whereby companies not complying with corporate governance codes are required to provide explanations for each item of non-compliance. This paper develops a typology for examining the rhetorical strategies companies use to persuade audiences of the need to explain rather than comply. Employing a meaning-oriented content analysis approach, the typology is applied to analyse explanations for non-compliance with the UK's Corporate Governance Code. The sample comprises non-compliance explanations of UK FTSE 100 companies over two periods (2004/05 and 2011/12). These periods were chosen as they follow substantial changes made in the UK's 2003 Code and 2010 Code. There were 63 (43) (2004/05 with 2011/12 in brackets) companies not complying with one or more provisions of the Code and 146 (71) explanations for non-compliance. Key rhetorical strategies identified in non-compliance explanations include 'minimization of negative feelings' (the damage is not too serious), the use of 'weasel words' which disguise non-compliance and 'transcendence' (ends justify means). The research shows there is increased use of rhetorical strategies in non-compliance explanations in 2011/12 compared with 2004/05, and the strategies found seem more orientated towards misleading explanations than meaningful convincing rationales. The use of such strategies may lead to mistrust by the market or may damage the 'comply-or-explain' system itself. Valid explanations are critical to the working of the 'comply-or-explain' system. Understanding the use of rhetoric can be helpful in assessing those explanations.

© 2017 Elsevier Ltd. All rights reserved.

1. Introduction

The 'comply-or-explain' system is premised on the inflexibility of a 'one-size-fits-all' approach. Under the 'comply-or-explain' system,¹ companies not complying with corporate governance code provisions are required to provide explanations. The 'comply-or-explain' system introduces some flexibility for companies (Roberts, 2012, chap. 9) or what Veldman and Willmott (2016) term "reflexivity" – continuous, self-organizing improvement of regulatory practice. As Haxhi and Van Ees (2010) observe, an explanation is more than disclosure of non-compliance, highlighting that German soft law codes only require disclosure of non-compliance without motivation, compared with the Netherlands and the UK which require

* Corresponding author.

E-mail address: Philip.Shrides@northumbria.ac.uk (P.J. Shrides).

¹ Sergakis (2015) questions whether 'one concept fits all'.

<http://dx.doi.org/10.1016/j.cpa.2017.08.003>

1045-2354/© 2017 Elsevier Ltd. All rights reserved.

Table 1
Historical development of the 'comply-or-explain' system.

Source	Description of system
Cadbury Report (1992, para 3.8)	... to state whether they are complying with the Code and to give reasons for any areas of non-compliance (para 1.3) ... but areas of non-compliance will have to be dealt with individually
Greenbury Report (1995, p. 13)	Include ... a general statement about their compliance ... which should also <u>explain and justify</u> any areas of non-compliance
Hampel (1998)	companies should be prepared to review and <u>explain</u> their governance policies, <u>including any special circumstances</u> which in their view justify departure from generally accepted best practice
Combined Code (1998, p. 1)	the company will be required either to confirm that it complies with the Code provisions or – where it does not – provide an explanation. Again, it must be for shareholders and others to evaluate such explanations.
Higgs Report (2003, para 1.14)	Listed companies have to report on how they apply the Code's principles and to state whether they comply with the detailed provisions and, <u>if not, why not</u> .
Combined Code (FRC, 2008, page 2), UK Corporate Governance Code (FRC, 2010)	If a company chooses not to comply with one or more provisions of the Code, it must give shareholders a careful and clear explanation ... In providing an explanation, the company should aim to <u>illustrate how its actual practices are consistent with the principle</u> to which the particular provision relates and contribute to good governance.
(FRC (2012b, p. 3, p. 6)	In providing an explanation, the company should aim to illustrate how its actual practices are both consistent with the principle to which the particular provision relates and contribute to good governance ... It should set the context and historical background, should give a <u>convincing rationale</u> for the action it was taking, and describe mitigating action to address any <u>additional risk</u> and to maintain conformity with the relevant principle. Also the explanation should indicate whether the deviation from the Code's provision was limited in time and when the company intended to return to conformity with the Code's provision.

disclosure to be accompanied by an explanation. Explanations are key to the 'comply-or-explain' system and thus are worthy of careful examination. However, the system is only as good as the explanations provided by companies.

Study of non-compliance explanations is important in judging the effectiveness of the 'comply-or-explain' system, given the continuing debate as to whether the voluntary nature of the system really works and criticism of the quality of explanations as being "perfunctory", "incomplete" or even "inexistent" (Sergakis, 2013, p. 397). Merkl-Davies and Brennan (2017) comment that silence may be a particular tactic in relation to soft-law disclosures, where there is little or no oversight by regulators. For example, not providing an explanation of non-compliance under the 'comply-or-explain' provisions of corporate governance codes (i.e., the rhetoric of silence) may create the impression of compliance. A critical perspective is appropriate, as non-compliance explanations are part of what Gendron (2016, p. 10) calls "the constellation of hopes and expectations" around corporate governance and as such may involve the constitution and propagation of myths.

It is useful to consider what is meant by the term 'explanation'. "Explanations occur whenever attention moves beyond the mere offering of information to matters of meaning, relationships, causes, factors and reasons" (Aerts & Theunisse, 2001, pp. 91–92). Explanations are likely to be deficient if they "fail to ... hang together" (Keil, 2006, p. 239). Table 1 summarises the historical development of the 'comply-or-explain' system in the UK to obtain insights into regulatory expectations underpinning the concept.² The Cadbury Report (1992, para 3.8) recommended 'reasons' for non-compliance be disclosed. The Greenbury Report (1995, p. 13) required companies to "explain and justify" non-compliance. The Hempel Report (1998, para 1.11) required the explanation to reflect "any special circumstance". The Combined Code (1998, p. 1) and the UK Corporate Governance Code (FRC, 2010, p. 4) specified that the explanation should be "careful and clear" and "illustrate how its [the company's] actual practices are consistent with the principle". Finally, the FRC (2012b) positioned explanations as rhetorical devices by introducing the notion of "convincing" explanations. The implicit assumption in the 'comply-or-explain' system is that "failure of governance can be remedied through yet more transparency" (Roberts, 2009, p. 962). Roberts' questioning of transparency as a regulatory instrument of accountability contrasts with the FRC's (2012b, p. 6) self-congratulatory view of the 'comply-or-explain' system as "widely admired and imitated internationally". The challenge, as observed by Tremblay and Gendron (2011, p. 260), is that "prescriptions have limitations since they are necessarily interpreted and enacted by complex and oftentimes unpredictable human beings". Tremblay (2012) characterises corporate governance regulations as symbolic, only ceremonially adopted, yet strengthening people's view of social order such that they create "illusions of control" (p. 395). Highlighting the "portrayal gap" of corporate reporting, Boiral (2013, p. 1038) reflects on the misleading relationship between publicly available corporate information and, referring to misleading images and representation, simulacra used to camouflage problems and project an idealised view of the firm.

Shortcomings in the quality of explanations have been identified by both academics (Arcot, Bruno, & Faure-Grimaud, 2010; Rose, 2016) and regulators (European Commission, 2011), with the Financial Reporting Council (FRC) (2013, p. 2) stating that "the variable quality of explanations remains its [the UK Corporate Governance Code's] Achilles heel". The Bank of England Executive Director for Financial Stability, Haldane (2012, p. 7), observes that with complex regulations, managers may "manage to the rules" rather than applying the spirit or substance of those rules "focussing on the small print at the expense of the bigger picture". Keay (2014) questions whether, in providing explanations, boards of directors are motivated

² The first reference we could find of usage of the phrase 'comply-or-explain' was by Kay (1992), commenting on the Cadbury Report (1992).

Download English Version:

<https://daneshyari.com/en/article/7412112>

Download Persian Version:

<https://daneshyari.com/article/7412112>

[Daneshyari.com](https://daneshyari.com)