Research Article

Konstantinos Sergakis*

A Rejoinder on Mr. Duhamel's Commentary

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Fair is foul, and foul is fair

Hover through the fog and filthy air

Shakespeare, Macbeth [Act 1.1.11–12]

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Introduction

Mr. Duhamel has commented on the interpretative complexities surrounding the 'comply or explain' principle, especially with regard to the following two points: whether the principle itself effectively offers a 'one concept fits all' approach and whether it is quintessentially a Pascalian wager.

*Corresponding author: Konstantinos Sergakis, School of Law, University of Bristol, Queen's Road Wills Memorial Building, Bristol BS81RJ, UK, E-mail: Konstantinos.Sergakis@bristol.ac.uk

The ‘one concept fits all’ dimension of the ‘comply or explain’ principle

With regard to the ‘one concept fits all’ approach, as mentioned in our paper, expectations and pragmatic considerations may very well differ depending on the relationship between the various parties involved, namely companies and service providers towards investors. Although it is true that the principle itself can be used in various frameworks and be adapted to very different circumstances, managing parties’ ‘expectations’ is the distinctive feature in this area, which makes us more doubtful of the holistic nature of the principle. In other words, expectations of regulators and investors with regard to a company’s or service provider’s statement is not expected to be identical given the nature of the information providers’ respective role in the market.

If this assumption is commonly acceptable, rates of compliance stemming from various parties’ statements should be interpreted and valued in a different way. Consequently, the ‘acceptance of non-compliance’ culture will inevitably develop differently depending on the framework where the ‘comply or explain’ principle is applied. Acknowledging that the principle itself provides a ‘one concept fits all’ approach may lead to the risky conclusion that expectations should be similar regardless of the identity of the provider of information. This can, in turn, multiply the superficial treatment of statements and lead either to a virtually automatic approval of compliance statements or an unreasoned rejection of non-compliance statements across the board.

This may also have overall ramifications on the way we perceive compliance (and non-compliance), especially with regard to the educational efforts that our paper seeks to develop. If our goal is for investors to change their behaviour in the future, the flexibility of the principle should not be interpreted as a ‘one concept fits all’ approach exactly in order to avoid the risk of people having similar expectations based on a widely applicable framework that is understood in a roughly identical way independently from the identity of the disclosing entity. Instead, our goal should be to encourage all parties to interpret statements in a more targeted way and, hence, be ready to evaluate ‘non-compliance’ in its proper dimension.

The Pascalian wager idea

Most importantly, the Pascalian wager idea risks shifting the focus from the development of possible practical solutions towards the simple observation that the outcome of all scenarios is uncertain. Although nothing can be argued with

certainty, hence the interest in using the Pascalian wager idea, we firmly believe that the principle itself can offer much more both to the providers and recipients of information disclosed in becoming a driver for change. The wager also implies that it is only under the condition that investors change their behaviour that the 'comply or explain' principle will become more effective: this hypothesis is, in our view, even more unpredictable and unlikely to occur in this framework if we do not accompany it with an 'institutionalised dialogue spectrum' as described in our paper.

Moreover, Mr. Duhamel seems to believe that the possible losses incurred should the 'comply or explain' principle prove useless would be minimal:

we aren't certain about its usefulness, but there is no clear-cut reason to abandon it! At worst, it is neutral and ineffective; at best, it will be an effective tool if investors ever decide to become long-termist and to develop a regular dialogue with companies...

From our viewpoint, the 'comply or explain' principle cannot be a wager because, if it proves to be useless, there will be clear losses in the overall regulatory spectrum: the legitimacy of the principle will be inevitably questioned and might also lead towards its abolition in the future, thus depriving corporate governance of flexibility and space for dialogue that cannot be conducted in the same way in the presence of a hard law framework.

It should be borne in mind that the principle itself is a 'meta-legitimation mechanism' in that it invites monitors to make judgments, not only on the legitimacy of regulatee action but also on the overall legitimacy of the underlying code and its provisions.¹ Therefore, our paper goes beyond the wager and seeks to strengthen the principle and add a further element on its usefulness by interpreting it not just as a simple dialogue framework that will work under the condition that investors will at some point – at least in theory – change their behaviour, but as a driver for change so that a behavioural shift will occur and make dialogue more fruitful for all parties involved.

Therefore, acknowledging that in our opinion the losses can be much greater than the ones mentioned above, the 'comply or explain' principle needs to be empowered by Review Panels that will have the task to deal with all the above-mentioned issues and endeavour to shape the foundational grounds for a possible change of market participants' behaviour in the future. While this task may appear idealistic or very optimistic, it is our firm belief that the 'institutionalised dialogue spectrum' does have a role to play in conjunction

¹ Paul Sanderson, David Seidl and John Roberts, 'The Limits of Flexible Regulation: Managers' Perceptions of Corporate Governance Codes and "Comply or Explain"', (2013) Centre for Business Research, University of Cambridge Working Paper 439/2013, 4.

with the ‘comply or explain’ principle itself, which can be now used – for the first time – in that direction. Exactly because we have used flexibility to allow market participants to disclose freely their compliance or non-compliance, now the time has come to start discussing both ideological stances and trigger a more engaged behaviour out of this dialogue. In the absence of any other concrete solutions that may lead to behavioural change in the markets, this may well be a humble start to serve as the ground for a new investment era.

Note: “The ‘Comply or Explain’ as a Pascalian Wager”, in this journal issue.