Legislating Corporate Social Responsibility in Kenya's Extractive Industry: A Case study of the Mui Coal Mining Project

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Abstract

Corporate governance scholarship, so far, has focused on a rather narrow, finance-dominated, agency theory perspective. This has been the case even in defining corporate social responsibility (CSR). Corporate social responsibility has only been justified where it is considered to be financially beneficial to the company. It is on that basis that this article addresses the question of whether such a paradigm is justifiable when applied to developing countries such as Kenya. The article is a case study of CSR in Kenya's mining industry that is dominated by multinationals. In particular, it focuses on the treatment of stakeholders in the Mui Coal Mining Project in Kitui County, Kenya.

Introduction

Corporate governance scholarship, so far, has focused on a rather narrow, finance-dominated, agency theory perspective. Directors of the company are described as 'agents,' and shareholders are described as the 'principal.' One of the principal assumptions of the agency theory is that the goals of the principal and the agent conflict, thereby necessitating an assumption that the primary objective of any form of regulation affecting the company will be to secure shareholders wealth maximization. This assumption is also evident in the definition of corporate social responsibility. It is observed that corporate social responsibility has only been justified where it is considered to be financially beneficial to the company.

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This proposition stems from one of the basic tenets of common law, which is that a director owes his duties to the company, usually interpreted as the shareholders.[1] In some instances, English courts have treated the acts of directors, in pursuing objectives which are not in the interests of the company or its shareholders as a whole, as going beyond the scope of the legitimate business for which the company was formed and, therefore, as being beyond the powers of the company and consequently totally invalid.[2] For example, in *Hutton v West Cork Railway Co*,[3] a company sold its assets and continued in business only for the purpose of winding up. Whilst it was awaiting winding up, a resolution was passed in the company's general meeting authorising the payments of a gratuity to the directors and dismissed employees for their past services to the company. The Court held that as the company was no longer a going concern such a payment could not be reasonably incidental to the business of the company and, therefore, the general meeting resolution was invalid. Bowen LJ in his ruling in *Hutton v West Cork Railway Co*,[4] described the director's obligation to shareholders as follows:

> [T]he directors of the company, might send down all the porters at the railway station to have tea in the country at the expense of the company. Why should they not? It is for the directors to judge provided it is a matter which is *reasonably incidental* to the carrying on of the business of the company; and a company which always treated its employees with Draconian severity, and never allowed them a single inch more than the strict letter of the bond, would soon find itself deserted – at all events, unless labour was very much more easy to obtain in the market than it often is. *The law does not say that there are to be no cakes and ale, but there are to be no cakes and ale except such as are required for the benefit of the company* …[5]

Bowen LJ's ruling in *Hutton v West Cork Railway Co* suggests that, directors are under a fiduciary obligation to exercise their powers over the management of the resources of the company in order to promote the interests of the company. In addition to this, the directors are only permitted to consider the interests of stakeholders in so far as they have a bearing on the

[1] Customarily, English law requires directors to act in the company's 'best interest' and that interest is usually interpreted as being the interest of shareholders of the company as a whole. See *Piercy v S Mills and Co* [1920] 1 Ch 77; *Hogg v Cramphorn Ltd* [1967] Ch 254; *Bamford v Bamford* [1970] Ch 212.

[2] RR Pennington, *Directors' Personal Liability* (1987) 59.

[3] *Hutton v West Cork Railway Co* (1883) 23 ChD 654.

[4] Ibid.

[5] Ibid 672 (emphasis added).

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company's interests. As shareholders are generally interested in getting the maximum return for their investment, the decision in *Hutton v West Cork Railway Co* suggests that directors in England are expected to see shareholder value maximisation as being the sole objective of the company.

A number of decisions in the law of trusts support shareholder-primacy as the objective of the company in the common law world. One such decision is Sir Robert Megarry VC's ruling in *Cowan v Scargill.*[6] The case of *Cowan v Scargill* concerned the exercise of powers and duties of the investment of trustees of a mineworkers' pension scheme. Ten trustees were appointed to administer the investment, five from National Coal Board and five from the National Union of Mineworkers. A formal investment plan was set up, but the five union trustees on the committee of management raised objections to investments in oil, investments overseas, and the acquisition of land overseas, and refused to concur in the adoption of the plan unless it was amended to take into account these objections, although they asserted that the benefit of the beneficiaries had been their sole consideration. The Court held that the duty of trustees was to act in the best interest of their beneficiaries and the power of investment had to be exercised so that the fund yielded the best return, regardless of the personal views and moral reservations of the trustees on the choice of the most suitable investments. Here, Sir Megarry VC interpreted the 'best interest' as being the one which offers the best financial interest to a beneficiary under a trust, and held that it would be wrong to subordinate considerations of financial returns to non-financial criteria, be they ethical, moral or political. In so doing, Sir Robert Megarry VC supported the norm of shareholder wealth maximisation as being the position of English courts on the objective of the company.

Ascertaining the objective of the company is important because it provides a clear goal against which a director's performance of his duties can be assessed. The decision of Sir Robert Megarry VC in *Cowan v Scargill* suggests that directors, as trustees of shareholders, act in breach of their duties to the company when they fail to *prioritise* the financial interest of the company.

On breach of fiduciary duties by trustees, Sir Robert Megarry VC wrote that:

[6] *Cowan v Scargill* [1985] Ch 270.

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> The duty of the trustees towards their beneficiaries is paramount. They must of course, obey the law; but subject to that, they must put the interests of beneficiaries first. When the purpose of the trust is to put provide financial benefits for the beneficiaries, as is usually the case, *the best interests of the beneficiaries are normally their best financial interests*. In the case of a power of investment, as in the present case, the *power must be exercised so as to yield the best return for the beneficiaries, judged in relation to the risks of the investments in question; and the prospects of the yield of income and capital appreciation both have to be considered in judging the return from the investment …* [emphasis added].

Therefore, English law makes room for consideration of non-financial factors such as stakeholder interests in the maximisation of shareholder value where ignoring stakeholder interests negatively affects the financial returns of the company. This position in English law is reflective of the Kenyan position on CSR as Kenya, being a former British colony, adopted its legal framework from England.[7] Kenya's position is thus: CSR is legal only if it can be demonstrated that it will result in a financial benefit for the company.

The problem with the current Kenyan position on CSR is that most of Kenya's companies in the mining sector are foreign owned and controlled. Maximising shareholder value in this respect means that Kenya gets little if any benefit from its natural resources, particularly its minerals. These mining companies often ignore the local community in the carrying out of their activities and there is no one to question them. Legally, the directors of these companies are not to consider the interests of stakeholders unless this is financially beneficial for the company. This state of affairs is evident in the Mui Coal Mining Project in Kitui County which shall be discussed below.

An Overview of the Mui Coal Mining Project in Kitui County

Prospecting for coal in Kitui County began, as is the case with most other minerals in Kenya, around 1999. The discovery of coal was made in 2010 when commercially viable coal deposits were found across four mining blocks in what were then Mwingi and Kitui districts. The

[7] Since Kenya was a British colony, the laws that the British exported to Kenya were mainly English laws. See section 3 of the Judicature Act, Chapter 8 of the Laws of Kenya. English law is thus considered to be highly persuasive in the Kenyan context. English law prior to 1897 is considered to be Kenyan law. Thus the 1883 decision in *Hutton v West Cork Railway Co* reflects the Kenyan position on CSR.

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Government then tendered for the mining of the coal with a Chinese corporation, Fenxi Mining Company, in conjunction with Great Lakes Company, a Kenyan corporation, winning the contract to extract coal from two of the four blocks. Fenxi owns a 89% interest in the Mui Coal Mining Project, with the Government owning 11%.[8] The economic importance of the Kitui coal mines is that the Mui Basin is estimated to hold 1 billion tonnes of coal with a potential to produce over 3,000 megawatts of power annually and is valued at 6.9 trillion Kenya Shillings (Kshs). The Government intends to use the power generated by the power plants to run the ambitious Kenya-Uganda standard gauge railway line with plans for, amongst other purposes, the introduction of Kenya's first electric train service. According to the mining agreement signed between Fenxi Mining Company and the Government, Fenxi will be allocated 10% of the mining interest in the Mui Basin. Fenxi will also cede 23% of its mining production to the Government as part of meeting local ownership requirements.[9]

Little is known about the ownership structure of Fenxi Mining Company and much less about the Great Lakes Company. Formed in 1956, Fenxi Mining Company is a subsidiary of a Shanxi Coking Coal Group, a Chinese corporation, which owns six other subsidiaries whose assets are estimated to be over 6 billion United States Dollars (USD), which is equivalent to Kshs 510 billion. The Company was one of 82 pilot enterprises founded by the Chinese Government. The Group was, however, privatised and listed on the Shanghai Stock Exchange in 1996. This Shanxi Group runs over 32 mines exporting coal to 6 countries across the world, including Brazil, Japan and Germany. It is the second largest coal coking company in the world, producing over 100 million tonnes of coal annually with total sales of over 9.85 billion USD (Kshs 833 billion) annually.[10]

The mining process in the Mui basin has stalled due to vast community objections to the mining project. The main contentious issue has been the land compensation process, and with the majority of those living in the mining zone holding no title deeds, it is difficult to establish land ownership. The Government has since started the process of demarcating the land and issuing titles. The residents of Mui have, however, felt shortchanged as they have not been involved in

[8] See, Kenya Broadcasting Corporation, 'Fenxi Mining Group and Coal Mining in Kenya Part 1- 4' <http://youtu.be/YgiYl3pHL2s> accessed 3 March 2015.
[9] See generally, Citizen Television, 'Who Own Kenya: Coal Mining Mui Basin' <http://youtu.be/vzdriKEIHJ8> accessed 3 March 2015.
[10] Kenya Broadcasting Corporation (n 8).

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the relocation and compensation plans. Consequently, Mui residents have on various occassions vowed not to cooperate until a liaison committee which consists of representatives from the four prospective blocks is involved in the talks. It is of concern that up until the final stages of negotiating the agreement between Fenxi Mining Company and the Government, stakeholders were not involved.[11] This is a violation of the Constitution of Kenya which provides for stakeholder engagement.

Article 62(3) of the 2010 Constitution of Kenya states that minerals shall vest in and be held by the national government in trust for the people of Kenya. The protection of the environment and natural resources is a function of the national government.[12] In article 69(1)(a) of the Constitution, an obligation is placed upon the State to ensure sustainable exploitation, utilisation, management and conservation of natural resources. Stakeholder engagement is emphasised in article 69(1)(d) of the Constitution, which provides that the State shall 'encourage public participation in the management, protection and conservation of the environment …' The residents of the Mui Basin, therefore, have a right as members of the public to be fully informed on the activities of Fenxi Mining Company, and the effects that its activities will have on their environment, and in particular the management of externalities such as health risks that are often associated with mining that could result from Fenxi's mining activities. Article 71 of the Constitution goes on to state how agreements relating to natural resources should come about. Article 71 is clear that such a 'transaction is subject to ratification by Parliament' if it involves the grant of a right or concession by or on behalf of any person, including the national government, to another person for the exploitation of any natural resource of Kenya.[13]

The coal mining agreement between Fenxi Coal Mining Company and the Government is a transaction that is subject to ratification by Parliament, without which it is null and void. To date, there has been little information on the process that resulted in the awarding of the mining tender

[11] See generally Kenya Television Network, 'Coal Mining' < http://youtu.be/WKFmbY7XzjQ> accessed 3 March 2015.

[12] See schedule four, part 1, clause 22 of the Constitution of Kenya (promulgated 27 August 2010) <http://www.kenyalaw.org:8181/exist/kenyalex/actview.xql?actid=Const2010> accessed 3 March 2015.

[13] Ibid article 71(1).

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to Fenxi Mining Company. Proper procedure was not followed resulting in claims that the tender was irregularly awarded.

Stakeholder engagement is the systematic and proactive integration of feedback from those impacted by an organisation's operations. In this case, Fenxi Mining Company should have sought the views of Mui residents, who will have to relocate, in coming up with an adequate compensation package. Stakeholder engagement means building trust even between those with different views. Arguably, had the residents of Mui been kept abreast of the activities of Fenxi Mining Company, the mining project would have proceeded on smoothly and the negative publicity, including claims that the mining tender was irregularly awarded, would have been avoided. Lack of stakeholder engagement in the mining industry is a serious issue that is often relegated to the background by mining companies and regulators. This is evident in Kenya's current mining laws, which are contained in the Mining Act of 1940, and which does not provide for public participation. Kenya's mining law have been under-review since 2013. The objective of this review is to give effect to the current Constitution's provisions on mining. No new laws have been passed so far.

Aside from the controversy surrounding the Mui Coal Mining Project, such a venture promises various benefits both at the county and national levels. At the county level, it will provide jobs for the community living in and around the Mui Basin, and on a national level, it will enable the country achieve its Vision 2030 objective,[14] through increasing its production of affordable and reliable energy to Kenyans. Other benefits that are said to result from this project for Kitui County are the setting up of a power plant and the related infrastructure, schools, residential houses, roads, shopping malls, health facilities and the construction of an airport, as has been the case in Inner Mongolia, an autonomous region in China, where Fenxi Mining Company is also extracting coal.[15]

A legal framework that protects the investors' interest is often deemed to be adequate by regulators. The question that is often left unanswered concerns who has the duty to protect the

[14] Kenya's Vision 2030 covers the period between the years 2008 to 2030 and aims at transforming Kenya into a newly industrialised middle-income country. See Government of Kenya, *Vision 2030, a Competitive and Prosperous Kenya* (2007).

[15] Kenya Broadcasting Corporation (n 8).

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interests of stakeholders, in this case, the residents of the Mui Basin. Whilst the residents of Mui have to weigh the benefits, and costs to them, of the coal mining project, it remains the regulator's role to protect the public interest. Regulators need to deal with the issue of how to regulate the multinational companies in Kenya's mining industry to ensure the protection of the public interest, more so in cases where the ownership structure of these companies is concentrated in favour of the company's home state. The titanium mining project in Kwale County, for example, is being undertaken by Base Resources Company, an Australian firm, through its local subsidiary Base Titanium Resources. Base Titanium Resources is fully-owned by an Australian company, that is, Base Resources Limited, which is listed in the Australian Securities Exchange. Base Titanium Resources has no Kenyan shareholders. However, a group of local asset managers and pension funds are said to have, in early 2013, acquired a 1% shareholding in Base Titanium's parent company, Base Resources Limited, which is valued at 170 million Kenya Shillings.[16]

Another example of a concentrated foreign ownership structure in Kenya's mining and extraction industry is that of Tullow Oil, the Company that is leading the Oil Exploration Project in Turkana County. Tullow has primary listing in the London Stock Exchange, and is a constituent of the Financial Times Stock Exchange (FTSE) 100 index. Institutional investors constitute over 87% of its shareholding: the institutional investors in the United Kingdom (UK) own 49.11%, the rest of Europe holds 14.38%, North America owns 19.11%, Asia accounts for 4.36% representation while the rest of the world, which includes Africa, accounts for 0.32%.[17] This provides a lot of food for thought for Kenya, which is the owner of the natural resource yet the least likely beneficiary from in the mining and extraction projects illuminated so far. Arguably, even when multinationals come in with the claim that they are providing 'assistance'– in the form of infrastructure that will facilitate development that will result from the venture, such as the Mui Coal Mining Project, there is the question whether that right to provide assistance includes certain responsibilities to the community. The bottom line is that natural resources should be utilised for the benefit of the people of Kenya.[18]An adequate regulatory framework has to, therefore, balance the interests of both investors and stakeholders, more so

[16] See generally, Base Resources, 'Base Resources' <http://www.baseresources.com.au/> accessed 3 March 2015.
[17] See generally, Tullow Oil, 'Tullow Oil Plc' <http://www.tullowoil.com/> accessed 3 March 2015.
[18] Article 69(1)(h) of the Constitution of Kenya (n 12).

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where the balance of bargaining power is tilted in favour of investors as is the case in Kenya's mining industry where the ownership structure of most – if not all - companies is concentrated, with the majority shareholder being a foreign entity.

It is a fundamental notion in legal theory that the powers of the corporation must be exercised in a way that benefits the corporation as a whole.[19] This fact is based on the shareholder view of the corporation. Berle, the pioneer of the shareholder view of the corporation, in his 1931 paper argued that:

> [A]ll powers granted to a corporation or to the management of a corporation, or to any group within the corporation, whether derived from the state or charter or both, are necessarily and at all times exercisable *only* for the ratable benefit of all the shareholders as their interest appears.'[20]

Berle was referring to the apparently unlimited powers conferred on corporate managers by the then recently enacted corporate statutes and charter provisions.[21] Whilst it is a fundamental notion in legal theory that the powers of the corporation must be exercised in a way that benefits the corporation as a whole, it is also accurate to say that in the case of the company's involved in Kenya's mining sector, the benefit of the corporation as a whole will translate to the benefit of the majority shareholder. Berle recognised this problem and, therefore, argued that the powers granted to the majority must be treated with the same regard as those granted to management.[22] He also stated that while the majority shareholders are not expected to act in a fiduciary capacity, they must not act in such a way as to suppress the minority shareholders.[23] According to Berle, a director is a trustee for shareholders, and a majority shareholder is in much the same position as a trustee.[24] Berle's argument that majority shareholders are trustees for minority shareholders implies that majority shareholders must fulfil the roles of a trustee. Sealy and Worthington identified that role as being to conserve the property of the beneficiaries.[25] Therefore, in a mining

[19] See AA Berle, 'Corporate Powers as Powers in Trust' (1931) 44 *Harvard Law Review* 1066.

[20] Ibid 1049.

[21] JL Weiner, 'The Berle-Dodd Dialogue on the Concept of the Corporation' (1964) 64(8) *Columbia Law Review* 1458.

[22] Berle (n 19) 1067.

[23] Ibid 1068.

[24] Ibid 1071.

[25] See generally L Sealy and S Worthington, *Cases and Materials in Company Law* (8th edn, 2008) 273.

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industry where licensed companies have a concentrated ownership structure such as in Kenya, these majority shareholders must conserve the property of the company on behalf of the beneficiaries, in this case, the national government and the county government. Doing so ensures that Kenya benefits from the mining and extraction of its mineral deposits. In addition, the chief purpose for the introduction of the concept of a corporation in Kenya was to provide a tool through which economic development could be achieved.[26] Concentrated ownership, however, seems to hinder economic development in a country whose mining industry is dominated by foreign multinationals, as directors will usually act in the interests of the majority shareholder; usually based in home state. The majority shareholders, based in the home state, can be said to be shadow directors[27] of these companies and, therefore, subject to the same duties and liabilities as their directors are subject to in the home state. In most of these countries where Kenya's mining multinationals originate from, especially in Canada and Australia, the directors of the mining companies would care about CSR if undertaking mining ventures there. There is, therefore, the question why CSR is not that important when the multinationals are mining in foreign states. Arguably, this is due to the limits of jurisprudence in the application of company law in the host state.

As much as holding the majority shareholder liable is an attractive concept to ensure that multinationals in developing states act in a manner that is socially responsible, such an action is dependent on the recognition of the concept of shadow director. The concept of shadow director has not been adopted in most African countries that adopted the common law system, including Kenya. However, some common law countries such as Nigeria have reformed their laws to include the concept of shadow director.[28] In most of the other African states that adopted the common law system, the law remains the same as it was at the time of inception. This is because a significant number of the majority shareholders in Kenya's public listed companies are politically connected, and as direct beneficiaries of such companies, have no incentive to reform

[26] See generally, Republic of Kenya, *Sessional Paper No 10 on African Socialism and its Application to Planning in Kenya* (1965).

[27] A shadow director is a person in accordance with whose directions or instructions the directors of a company are accustomed to act. In short, a shadow director is anyone who is directly calling the shots in a company for example, a majority shareholder.

[28] See generally, S Robinson, 'United Kingdom: Getting the Deal Through' *(*2007) *Corporate Governance* 216 at https://www.gettingthedealthrough.com/ .

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the law which currently protects their interests.[29] Kenya thus suffers from rent-seeking, resulting in regulatory capture[30] in the area of corporate law. Rent-seeking is rife in the mining and extraction sector.

Rent seeking occurs where individuals expend time, money and other resources competing for a fixed amount of wealth, in effect squabbling with each other over the size of their individual pieces of a fixed group pie.[31] The tragedy in Kenya is that there is tendency to do the housekeeping when the visitor has already arrived. As long as mining and extraction legislation is reviewed and enacted while the interested parties, and the envisaged activities, are already underway, corruption or interference leading to corruption and self-interest is bound to take place. The tragedy is that, although the rent seekers may have regulatory roles by virtue of being in public office or position (or having access to such an office or position), their motivation is to maximise their personal interest rather than the national interest. As long as the multinational can pay off the rent-seeker, he will cede interest in the natural resource, which will be plundered for the benefit of a few local individuals and the home state of the multinational resulting.

It is important that on a national level, Kenya's legislature devotes most of its time reviewing out dated laws and enacting new legislation – in advance of any mining or extraction activity - for the benefit of posterity, without necessarily being guided by self-interest or the interests of the participating parties. Rent-seeking is itself costly and can erode and even destroy the economic gains that flow from foreign investment. The net result of rent-seeking in Kenya's mining and extractive industry is to reduce the total revenue available for distribution to the national and county government resulting from exploration activities.

As the notion of the corporation in Kenya was introduced for the main purpose of being a tool through which economic development can be achieved, Dodd's social responsibility view appears to be a possible basis which can guide reforms of the law affecting the mining sector in Kenya. Dodd acknowledged the traditional view that a corporation is an association of stockholders that is formed for their private gain, and which is to be managed with that end in

[29] See generally, LM Musikali, 'The Law Governing Directors in Kenya: A Comparative Review' (DPhil thesis, University of Manchester 2012); JK Mwaura, 'The Kenyan Regulation of Directors: An Analytical Study (DPhil thesis, University of Wolverhampton 2003).

[30] Regulatory capture occurs when a regulatory agency, created to act in the public interest, instead advances the commercial or special concerns of interest groups that dominate the industry or sector it is charged with regulating.

[31] MM Blair and LA Stout, 'A Team Production Theory of Corporate Law' (1999) 85(2) *Virginia Law Review* 250.

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view.[32] However, he pointed out that it is 'public opinion, which ultimately makes law,' and noted that there were 'substantial strides in the direction of a view of the business corporation as an economic institution which has a social service *as well as* a profit-making function.'[33]

The idea of taking into account 'other interests,' other than those of shareholders in decision making, is the essence of what has come to be known as the stakeholder theory. The stakeholder view of the company emerged from the work of Dodd and was further developed by Freeman. Freeman argues that a corporate manager's duty is to create optimal value for all social actors who might be regarded as having being affected by the company's decisions.[34] Within the social and economic view, all stakeholders have a right to be regarded as an end, but not as just a means to an end.[35] The stakeholder theory safeguards the interests of the community as a stakeholder in developing countries where foreign ownership of companies in the mining sector is dominant, such as in Kenya. This is because the stakeholder theory provides room for the interests of stakeholders, such as the community, to be considered equally and independently, not merely because of their ability to further the interests of a certain group such as shareholders, but because the decisions of the company affect their welfare. Keay notes that adopting this view tames the 'harsher aspects of capitalism', as no group is given priority over the other.[36]

In addition, regulation also has to be balanced so that it does not put off investors. Having investor friendly laws is critical for national development. The need for a balance has become clear in recent years, with investors airing concerns on proposals that the Government introduce legislation requiring a 35% local ownership in mining companies.

In sum, the controversy between local residents and investors in the mining industry in Kenya can be traced to the shareholder versus the stakeholder debate, and in particular a view once famously propounded by Milton Friedman, that the only real purpose of a company is to

[32] EM Dodd, 'For Whom Are Corporate Managers Trustees?' (1932) 45 *Harvard Law Review* 1146-1147.

[33] Ibid (emphasis added).

[34] Ibid.

[35] A Keay, 'Ascertaining the Corporate Objective: An Entity Maximisation and Sustainability Model' (2008) 71(5) *Modern Law Review* 674.

[36] Keay (n 35).

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make profits.[37] Following Friedman's view, there have emerged various schools of thought on whether the main purpose of a company is only to operate in such a way that it generates the maximum profits for its members, or whether it should take into account the interests of the society and, therefore, behave ethically in its day to day businesses. This has come to be referred to as the CSR debate.

The Corporate Social Responsibility Debate

The question, of '[t]o whom do directors owe a duty?' is contentious and at the root of the CSR debate. The answer to this question lies in company law. Companies in common law are seen as separate legal entities having their own personality,[38] and their directors are seen as fiduciaries who run the company on behalf of the corporation,[39] defined as current and future shareholders.[40] This implies that the directors owe their duty to shareholders. However, in recent years, the change in public opinion that Dodd talked about has become evident. In particular, a move towards the acceptance of CSR in common law jurisdictions has recently been observed, for instance, with the introduction, in England, of section 172 of the Companies Act of 2006. The legislation requires that directors conduct themselves in a way that they believe will promote the success of the company in good faith, while at the same time considering the long-term effect of their actions on other parties including the employees, the community and the environment, as well as the customers and suppliers. In addition to this, directors are obliged to ensure that while conducting the business of the company, the corporation upholds a high quality of business conduct while at the same time acting justly to members of the company. This has come to be known as the enlightened shareholder value (ESV). ESV is essentially:

> An obligation on directors to achieve the success of the company for the benefit of shareholders by *taking proper account of all the relevant considerations* for that purpose … [including] a proper balanced view of the short term and the long term, the need to sustain effective ongoing relationships with employees, customers and suppliers and

[37] M Friedman, 'The Social Responsibility of Business is to Increase Its Profits' *New York Times Magazine* (New York, 13 September 1970) 1.

[38] *Salomon v A Salomon and Co Ltd* [1897] AC 22.

[39] Keay (n 35).

[40] A company in English law is defined as shareholders present and future. See *Percival v Wright* [1902] 2 Ch 421.

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> others; and the need to maintain the company's reputation and to consider the impact of its operation on *the community and the environment*.'[41]

Although the concept of CSR is now a widely accepted concept, there is no consensus on the meaning of the concept. Various definitions have been put forth on the doctrine of CSR. According to Roberts, the concept of CSR is about the various strategies of a company that identify it as being concerned with the issues affecting society.[42] Waddock, goes further and describes the concept as the amount of responsibility that is shown in a company's policies, as well as in the manner in which it operates, and how these policies impact the natural environment and the stakeholders of the company.[43] Lord Holme and Richard Watts define the concept as, 'the continuing commitment by business to behave ethically and contribute to economic development while improving the quality of life of the workforce and families as well as the local community and the society at large.'[44] CSR has also been defined as being the doctrine through which companies conduct their business in order to achieve a positive impact in the society.[45] Consequently, it is evident that the purpose of CSR is to ensure that companies are run in a way that results in a positive impact in the society while at the same time earning a profit and behaving ethically. Stakeholders are progressively taking an interest in the good and bad practices of the company in terms of the services it provides, as well as how it treats its personnel and its effect in the community at large.[46]

CSR in practice is portrayed in different ways. In the United States, the concept is exemplified by companies through philanthropic giving, whereby corporations donate some of

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[41] Company Law Review Steering Group, *Modern Company Law: For a Competitive Economy - Developing the Framework* (March 2000) paras 3.30 - 3.31.

[42] J Roberts, 'Determinants of CSR Disclosures' (1992) 17.6 *Accounting, Organisations and Society* 595.

[43] S Waddock, 'Parallel Universes: Companies, Academics and the Progress of Corporate Citizenship' (2004) 109.1 *Business and Society Review* 10.

[44] R Holme and P Watts, 'Corporate Responsibility: Making Good Business Sense' (World Business Council for Sustainable Development, January 2000) <http://www.wbcsd.org/web/publications/csr2000.pdf> accessed 3 March 2015.

[45] M Baker, 'Corporate Social Responsibility – What Does It Mean?' (Corporate Social Responsibility, 8 June 2004) <http://www.mallenbaker.net/csr/definition.php> accessed 3 March 2015.

[46] Ibid.

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the profits to charities without anticipating any benefit from the donations.[47] In Europe, on the other hand, an emphasis is put on running the main business in a way that is socially responsible while at the same time investing in communities for reasons only pertaining to the business.[48]

Arguments against Corporate Social Responsibility

Despite the glaring need for corporate social responsibility, various arguments have been made against the notion of CSR, with proponents of shareholder value arguing that providing goods at an adequate price for customers is beneficial to society.[49] Furthermore, engaging in CSR defeats the entire purpose of the shareholder primacy theory as the concept is based upon the aim of generating maximum profits for the shareholder.[50] According to Friedman, considering the interests of other parties, instead of those of shareholders, creates a conflict of interest and constitutes a breach of duty,[51] as the director's position is contractual.[52] Whilst Friedman recognises that a director, as an individual, may have other voluntary responsibilities to his family or to charities and other causes, he argues as these are voluntary duties, and the director may pursue them at his own time using his own income. However, the director should not engage in these practices while he or she is acting as the agent of the shareholders as this goes beyond his duties to the shareholders.[53]

The main bone of contention on whether companies should engage in CSR is costs. First, directors of companies in the mining industry tend to see the requirement that they engage in CSR as being a form of political pressure that is costly to the company. Companies are seen as being pressured into taking part in community activities on the premise that they will gain profits in the end – however, in taking part in some of these activities, the companies are taking up the

[47] Ibid.

[48] Ibid.

[49] B Schaefer, 'Shareholders and Social Responsibility' (2008) 81 (2) *Journal of Business Ethics* 297.

[50] Ibid.

[51] Ibid.

[52] Friedman (n 37).

[53] Schaefer (n 49).

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responsibility of the government, and fulfilling government goals.[54] The building of social facilities in the community, and donations to the poor in society, are goals that governments need to fulfil on their own. However, governments encourage companies to use their funds to achieve these goals, which mean that while the company is making its decisions, it also needs to set aside a portion of its funds to help out in society. Secondly, activities that promote CSR are funded out of the gross profits that the company accrues before tax.[55] Therefore, costs are borne by both the shareholders of the company as it is they who own the company, and the government, as the costs are deducted before the company's profits are taxed.[56] This causes a problem because even though the company is performing a philanthropic deed, it is being conducted at the expense of other people:[57] the shareholders and the government.[58] This is arguably not beneficial to the shareholders who own the company, and stakeholders such as the state, who may consider other activities more beneficial or urgent in terms of profit or tax-spending, compared to the CSR activity chosen by the directors of the company.

Moreover, questions arise concerning who gives the directors the authority to make decisions regarding social and environmental issues, because the only provision made in law is that the directors owe duties to the company – defined as present and future shareholders - who want the company to produce maximum profits for them.[59] As there exists no legal guidelines that give directors the responsibility to perform philanthropic activities on behalf of the firm, directors who engage in CSR are seen as acting out of their own accord. Such directors may not even have the expertise required in the field of philanthropy that they have chosen to engage the company in. All these result in a conflict of interest upon the directors as they owe a duty to shareholders, and can only be resolved if there were regulations or guidelines set out to determine where the

[54] 'Radar: The Government Issue' (Sustainability, 1 June 2004) <www.sustainability.com/philosophy/who-we-are/default.asp> accessed 3 March 2015.

[55] F Robins, 'Why Corporate Social Responsibility Should be Popularised but not Imposed' (2008) 8 (3) *Corporate Governance* 330, 334

[56] Ibid.

[57] RB McKenzie, 'Corporate Failure as a Means to Corporate Responsibility' (1994) 12 *Journal of Business Ethics* 969.

[58] Ibid.

[59] Ibid.

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directors obtain the authority to perform philanthropic activities.[60] This in turn will increase the directors' confidence in the notion of CSR, as some directors may not engage in such activities for fear that they would be going beyond their assigned duties. It is, therefore, understandable when the directors and management of the mining companies in the Mui Basin are reluctant to engage in the CSR that is expected by the local community including the State.

Arguments for Corporate Social Responsibility

That said, the concept of CSR brings forth the noble idea that companies need to play an active role in the society – that of giving back to the society. This is due to various occurrences in the world today such as global warming and the change in climate, corporate scandals and a lack of unity in society.[61] Proponents of the CSR norm hold similar views as those held by supporters of the stakeholder theory, which, as we have seen, champions for directors to consider the interests of various parties, including the community in which the business operates.[62]

Proponents of CSR give various reasons as to why they support the concept. A leading argument for CSR is that there has been a societal and economic change from the traditional idea that companies should run in order to produce maximum profits for shareholders.[63] Instead, companies should aim at making contributions towards the surrounding community, by adopting sustainable choices in the day to day running of the corporation, as well as striving to elevate the living and working conditions of their employees, which will give the employees an incentive to work harder.[64] Secondly, directors of a company should seek to incorporate the interests of all the parties that may be affected by the decisions made by the company, namely, the employees, the creditors, the shareholders as well as the community.[65] This should be so because these other

[60] Robins (n 55) 335 -336.

[61] J Jonker and A Marberg, 'Corporate Social Responsibility *Quo Vadis*?' (2007) 27 *Journal of Corporate Citizenship* 107, 108.

[62] M Clarkson, 'A Stakeholder Framework for Analyzing and Evaluating Corporate Social Performance' (1995) 20 *Academy Management Review* 92, 112

[63] Jonker and Marberg (n 61).

[64] Ibid.

[65] E Freeman, *Strategic Management: A Stakeholder Approach* (1984).

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stakeholders also contribute towards the success of the company.[66] Supporters of CSR view the goal of maximising shareholder wealth as too narrow,[67] and champion for companies to engage in activities that embody CSR, as doing so increases publicity for the company and attracts more customers.

There are, however, some limitations in the arguments of proponents of CSR. Supporters of CSR, usually sympathisers of the stakeholder theory, fail to recognise the fiduciary duty that is owed by directors to shareholders, as the owners of the company, when they champion for the company to be run in such a way that all the interests of the stakeholders are considered. Additionally, the notion of CSR brings about competing interests in the company. This is because the directors have too many interests to consider as they make corporate decisions, and balancing the interests of all this parties is almost impossible.[68] Therefore, insisting on CSR can create even more problems within the company itself.

With regard to the issue of costs that was raised before, it is argued that CSR is beneficial to the company in the long run in that, as much as the company uses profits belonging to shareholders to fund the philanthropic activities, the corporation benefits in the long term.[69] The activities that the company performs in the community serve as an advertising tool which attracts customers and even investors to the corporation. However, it has been argued that there has been no proof that ties good financial performance with socially responsible behaviour.[70] Although certain studies show that companies which are considered as the most sustainable corporations engage in environmental and social philanthropy, it is difficult to tie good financial performance to CSR[71].

[66] E Freeman and D Reed, 'Stockholders and Stakeholders: A New Perspective on Corporate Governance' (1983) 25 *California Management Review* 88, 89.

[67] D Wood, 'Whom Should Business Serve?' (2002) 14 *Australian Journal of Corporate Law* 1, 13.

[68] E Sternberg, 'The Defects of Stakeholder Theory' (1997) 5 *Corporate Governance* 3, 6.

[69] Robin (n 55) 334.

[70] L Burke and J M Logsdon, 'How Corporate Social Responsibility Pays Off' (1996) 29(4) *Long Range Planning* 495.

[71] Robin (n 55) 334.

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The idea that CSR is a notion that is politically backed can prove to be beneficial to the company in as much as it is detrimental. When the companies take on the responsibilities of the government, and provide amenities for the community such as schools and hospitals, this works as a wakeup call for the government as the citizens will put pressure on the state to provide these facilities for the citizens of the country. This in turn will increase prestige for the company in the public eye, as customers may, as a result, be willing to engage in business with the company that has provided basic amenities for them rather than the one that has not.[72] This argument can, however, be said to be too theoretical when applied to the African context where citizens do not conventionally put pressure on governments, and thus, CSR may not induce positive government performance.

CSR is seen as a norm that is adhered to by companies which aim to change the corporate norms that are found within the environmental and social platform.[73] The voluntary engagement of companies in this process is influenced by widespread business principles. The companies aim to advance the concept of CSR as a standard of behaviour for private companies.[74] This, therefore, leads to the creation of a pro-active corporate culture which promotes the interests of the community as well as its own interests. Multinationals are unlikely to have an incentive to reform the standard behaviour of companies in the host state. That said, it cannot be gainsaid that engaging in activities that promote CSR can have good effects for the company. Once a company takes part in activities that promote the concept, the corporation avoids bad publicity and at the same time increases its business opportunities[75].

Conclusion.

This article has highlighted the fact that the CSR concept is a voluntary norm that is adopted by company directors who implement policies with the aim of taking part in shaping the society and the community at large.[76] This concept, however, is not widely accepted. Scholars and

[72]Burke (n 70).

[73] L Albareda, 'Corporate Responsibility, Governance and Accountability: From Self-Regulation to Co-Regulation' (2008) 9 *Corporate Governance* 430, 433.

[74] Ibid.

[75] Robin (n 55) 335.

[76] Jonker and Marberg (n 61).

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regulators, who often take an agency theory perspective to corporate governance, argue that the company should be run for the benefit of shareholders, and that the interests of other stakeholders are not a prerequisite, though they may be considered. This is because shareholders own the company, and thus require that the directors do all that they can do to ensure that the shareholders gain maximum profits from the corporation. Other arguments as to why the company should be run with the goal of maximising profits for the shareholders only centre around the costs incurred while implementing CSR. As we have seen, these costs are borne by the shareholders of the company, which is against the shareholder wealth maximisation goal. In addition to this, directors who take part in activities that promote CSR have no authority to do so from the shareholders to whom they are accountable. Consequently, we can conclude that although the requirement that companies engage in CSR is noble, it has no legal basis, necessitating the need for development of regulations at the national and international level.

In addition, for the citizens of developing countries such as Kenya to benefit from their mineral and oil deposits, it is important to recognise that paradigms such as the agency theory cannot be justifiably applied to such states, where the ownership of mining and extractive companies is both concentrated and predominantly foreign. Where such an ownership structure exists, reforms to the corporate law framework, such as the recognition of the concept of shadow director, are beneficial in ensuring that multinationals not only adhere to the concept of CSR when operating in the home state, but also when carrying out activities in the host state. In particular, this legislation should ensure that multinationals not only compensate the community financially when it has to be displaced, but also support the community through the transition. Developed states should also put positive pressure on governments in developing countries to respect CSR, by investing only in socially responsible investments. At a national level, it is important that in awarding mining tenders, the national government respects the Constitution, which provides for stakeholder engagement and requires that natural resources are used in a manner that is beneficial for Kenya as a nation, as well as for the residents of the county in which the resources are found.

In the meantime, Kenya's mining industry is not a lost cause. It is exigent that Kenya exercises due diligence in ensuring the enactment of an adequate legal framework to guide the exploitation of natural resources. Whilst it is the responsibility of the State to ensure that

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companies such as Fenxi Mining Company, Base Titanium Resources and Tullow Oil are accorded the necessary cooperation and provided with an enabling environment to do business, the Kenyan Government should also ensure that stakeholders such as the local community are protected from exploitation and marginalisation by foreign investors through the enactment and enforcement of laws that require such investors to adhere to CSR. If the State does not require that foreign investors adhere to CSR, it creates a potentially detrimental socio-economic situation. If Kenya is left with displaced and disposed people, as is the case in the Mui Basin, the State's poverty situation will be compounded. The residents of Mui will end up poorer than they were in their former habitat, bearing in mind externalities that are associated with mining. In coming up with compensation agreements, public participation is necessary. Compensation should be adequate. It should go beyond mere compensation of land to the residents of Mui and paying the state the market price of the minerals. It should include compensating residents for transition expenses and inconveniences, such as the costs of adapting to a change in livelihood as a result of relocation, and compensating the State for its goodwill in giving up its natural resources. In addition, the State, for the benefit of future generations, ought to be given an everlasting financial stake in the economic activities of foreign mining companies.

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