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Explanations for corporate governance non-compliance: A rhetorical analysis

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

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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.

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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

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

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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).

by what they can get away with. Veldman and Willmott (2016, p. 581) believe the Code is “infused by a ‘cultural grammar’ that . . . restricts accountability to narrow forms of information disclosure . . .”.

Non-compliance explanations have been analysed by reference to acceptability (Pass, 2006), specificity (Arcot et al., 2010; Hooghiemstra, 2012), arguments mobilized (Hooghiemstra & van Ees, 2011), legitimacy tactics (Seidl, Sanderson, & Roberts, 2013) and quality characteristics (Shrives & Brennan, 2015). This paper takes a different approach – looking instead at the rhetorical strategies applied by companies in persuading audiences of the explanations proffered. Explanations need to be persuasive/convincing in justifying non-compliance. The FRC (2012b, p. 6) identifies “a convincing rationale” as one of three elements of a meaningful explanation.³ In the case of non-compliance therefore, companies may be more likely to engage in rhetorical strategies, motivated possibly to persuade shareholders to concur with the explanation. This paper explores their use. We assess the extent to which the non-compliance rhetorical strategies are in line with meaningful, convincing rationales or whether they are more illustrative of superficial and misleading explanations. We recognize that each non-compliance disclosure can incorporate rhetorical strategies; the important point is whether or not they are sufficiently meaningful.

Persuasive and convincing explanations are critical to the legitimacy and effectiveness of the ‘comply-or-explain’ system. Sanderson, Seidl, and Roberts (2013, p. 6) argue that “legitimacy is clearly in part discursively constructed in texts”. We address three research questions (RQ) and examine explanations for non-compliance in UK FTSE 100 company annual reports to assess the extent to which rhetorical strategies are used (RQ 1). The study is carried out in 2004/05 and 2011/12. This enables a comparison of rhetorical strategies over the two time periods from the post-Enron 2003 version of the Code to the post-global financial crisis 2010 version of the UK Corporate Governance Code (RQ 2). We also assess the extent to which rhetorical strategies are used together (RQ 3).

This is the first study of the use of rhetoric in corporate governance non-compliance explanations. The paper makes four contributions to the prior literature: (i) It develops a typology of rhetorical strategies in corporate explanations for non-compliance with the UK Corporate Governance Code; (ii) It applies the typology to identify the use of different rhetorical strategies in the explanations; (iii) It compares the use of rhetorical strategies in explanations over two time periods and; (iv) It considers the extent to which rhetorical strategies in explanations are used together. Shrives and Brennan (2015) analyse non-compliance explanations against seven quality characteristics: (i) Location, (ii) Comprehensiveness, (iii) Originality/Mimetic behavior, (iv) Length, (v) Complexity, (vi) Specificity and (vii) Attestation. This paper takes Shrives and Brennan’s (2015) analysis of non-compliance explanations against a quality typology one step further by conducting a sentence-by-sentence analysis of the content of the explanations, focusing on the use of nine rhetorical strategies in our typology used by companies to persuade/justify their non-compliance.

This paper proceeds as follows: Section 2 considers persuasion in corporate reporting including relevant theories, rhetorical strategies and culminates with the typology in Section 3. Section 4 describes the research methods and is followed by results in Section 5. Finally, the paper concludes in Section 6 and provides suggestions for further research.

2. Theoretical framework

In this section, we examine prior conceptualisations of corporate governance from a rhetorical perspective. Rhetoric “is concerned with the modes of persuasion” (Aristotle, 350BC/2010, p. 5). We frame our analysis of corporate governance non-compliance explanations as a “critical rhetoric” of the language of compliance as a means to persuade shareholders and stakeholders, motivated by existing power relationships between corporates and their audiences. Our perspective is that corporate governance non-compliance explanations are socially constructed, and our focus is on the construction and communication of the explanations. Institutional theory (DiMaggio & Powell, 1983; Scott, 2014) can also be useful in analysing how these explanations are communicated to readers. Audiences for these explanations are unlikely to question compliance, which is seen as legitimate (Suchman, 1995) and so management has incentives by using rhetoric to make explanations for non-compliance appear equivalent to, or better than, compliance. Another approach is to attribute the non-compliance to an event beyond management’s control, thereby implying that someone or something else is to blame (attribution). We use Benoit’s (1995, 2015) image repair work to develop an appropriate typology by which to analyse and better understand these explanations. Although ‘comply-or-explain’ is often cited as one of the key strengths of the Code, it is in fact compliance that is most often reported on by the FRC and those monitoring the Code. Because of what we believe to be increasing institutional pressure to comply faced by companies over time, we expect a greater incidence of rhetorical strategies in the second time period (RQ 2).

We consider the relations of power. In the context of corporate governance non-compliance explanations, the power relations are that investors and stakeholders depend on management for information on corporate governance processes and procedures. Audiences do not know whether the rhetoric reflects the underlying corporate reality.

³ The other two suggested by the FRC (2012b, p. 6) are (1) to provide the context and historical background to the non-compliance and (2) any mitigating action(s) to address any additional risk and to maintain conformity with the overarching Code principle. Often perfunctory explanations do not address these and commonly affirm that the particular non-compliance is unlikely to do any damage without explaining why that is, or why non-compliance occurred in the first instance.

2.1. Rhetoric and corporate governance explanations

Rhetoric has been defined as the art of persuasion by words (Kennedy, 1991, as cited in Castelló & Lozano, 2011, p. 14). A study of the use of rhetoric by organizations can add insights to our understanding of the ways in which corporate reporting is used to influence audiences' interpretation (Brennan & Merkl-Davies, 2014). The use of rhetoric is more likely to be pronounced during shortfalls in corporate performance (Coupland, 2005; Suddaby & Greenwood, 2005), as organizations depend on public approval and thus need to 'engineer' public support (Bernays, 1947). Although corporate governance non-compliance *per se* is not a shortfall in performance, companies may be under pressure to justify their corporate governance choices. Analysing an issue from the perspective of a corporation's own words may provide new insights into corporate behavior (Fairfax, 2007). At the level of language use, common vocabularies, terms and rhetorical strategies may be prevalent and therefore of interest (Coupland, 2005). It is particularly appropriate to examine corporate governance explanations through a rhetorical lens, given their purpose being to provide a "convincing rationale" (FRC, 2012b, p. 6).

2.2. Compliance rhetoric and corporate governance explanations

The focus of analysis in this paper is on the use of rhetoric as a means of influencing audiences' opinions of explanations for corporate governance non-compliance. Suddaby and Greenwood (2005) describe rhetorical strategies as the deliberate "use of persuasive language" to legitimate (p. 35). In Section 3, we set out the specific rhetorical strategies chosen to study corporate governance non-compliance explanations. Tomasic (2011, p. 55, chap. 3) argues that corporate governance ["laissez-faire"] rhetoric serves to legitimize a self-regulatory approach. Beare (2005 p. 156, chap. 6) identifies a "compliance rhetoric" and the development of a language of compliance between corporations and a wider society. She argues that the rhetoric of non-compliance serves to protect the corporation and that such rhetoric "can be very strong and serve to obfuscate a reality of neglect" (Beare, 2005, p. 156). Thus, compliance rhetoric may be used as a means of maintaining the status quo. Parker (2000, p. 560) observes that there is a danger that compliance (and we would add non-compliance) rhetoric will be used merely to manage appearances, and that this is a competition for the confidence of persons faced with decisions as to where and how to act (Shearing, 1993, chap. 5). Laufer (2006, p. 247) considers the use of rhetoric in corporate governance serves to generate "creative and seductive illusions of corporate compliance and governance". In the context of risk management, Spira and Page (2003) observe that a techno-scientific approach forms the basis of a rhetoric that links risk management to good governance. They comment on a "rhetoric gap" (p. 657) where corporate governance standards may be substantially different to practice within organizations, which rhetoric gap in our context may, in turn, extend into written explanations of practice.⁴

Rhetoric may go beyond the mere use of language to persuade, to the manipulative/opportunistic use of language. Sophistry⁵ – "Specious but fallacious reasoning; employment of arguments which are intentionally deceptive" (Oxford English Dictionary Online, Oxford Dictionaries, 2016) – may explain the rhetoric-reality gap. Brennan and Turnbull (2002, p. 597) provide a useful discussion of sophistry, and management practices as sophistic and symbolic. To sum up, it is "winning of the argument that matter[s] and not the truth". Thus, those who engage in sophistry are opportunistic, manipulate audience sentiment and are not concerned with the substance of the argument. The lens of sophistry provides a useful additional perspective through which to view non-compliance explanations. Sensitivity to sophistry may cause readers to question the validity of explanations.

Drawing the themes in this section together, non-compliance explanations are essentially rhetorical devices, to persuade shareholders that non-compliance is legitimate and to support the 'comply-or-explain' system. Some rhetoric may go beyond mere persuasion, using more manipulative and opportunistic means of explaining non-compliance, i.e., 'sophistic'. Our empirical challenge is to develop a typology that reflects these theoretical points.

3. Development of a typology of rhetorical strategies in non-compliance explanations

The purpose of an explanation is (i) to provide "a convincing rationale" (FRC, 2012b, p. 6); (ii) to legitimize; and (iii) to protect the company's image to show that, despite non-compliance, the company has a full and robust system of governance. We borrow from the work of Benoit (1995), which we believe is an appropriate theoretical lens for viewing non-compliance explanations, as Benoit also analyses corporate explanations, in his case, for image-damaging events. We also include insights from Bolino and Turnley (2003) which we consider contributes a finer-grained analysis, including consideration of rhetorical strategies in combination. Thus, we analyse explanations for non-compliance by developing a typology of rhetorical strategies, from Benoit's (1995) image-restoration strategy and Bolino and Turnley's (2003) impression management profiles, adapting prior research for use in a corporate governance setting. Benoit (1995) classifies 14 image-restoration strategies into five categories as summarized in Table 2. We add Bolino and Turnley's (2003) five impression management profiles. A typology is, in essence, a classification scheme whereby items with similar characteristics are grouped together (Bailey, 1994). Like many research tools, they have advantages and disadvantages. Complexity in

⁴ We thank one of the reviewers for this point.

⁵ We thank one of the reviewers for suggesting this rhetorical perspective.

Table 2
Developing the typology.

<i>Benoit's (1995) image restoration strategy</i>	<i>Included ✓/excluded ✗ in our typology</i>	<i>Prior studies</i>
1. Denial		
(i) Simple denial	✓[Rhetorical Strategy 9] 'Concealment/Denial'	Goffman, 1971; Ware & Linkugel, 1973; Oliver, 1991; Abrahamson & Park, 1994.
(ii) Shift the blame	Someone else did it (see 5 (iii) below: Attribution)	Schonbach, 1980.
2. Evasion of responsibility		
(iii) Provocation	✗ Not applicable	*Note: Although these categories are in theory possible, the pilot study showed that in relation to corporate governance explanations by FTSE companies, they are unlikely, occurring rarely, if ever. Hence, they were excluded from the typology.
(iv) Defeasibility (Lack of information)	✗ Not applicable	
(v) Accident	✗ Not applicable	
(vi) Good intentions	✗ Not applicable	
3. Reducing offensiveness of event		
(vii) Bolstering	✓[Rhetorical Strategy 2]	Ware & Linkugel, 1973; Cheney <i>et al.</i> , 2004; Moerman & van der Laan, 2007; Bebbington <i>et al.</i> , 2008
(viii) Minimization	✓[Rhetorical Strategy 3]	Rosenfeld <i>et al.</i> , 1995; Bebbington <i>et al.</i> , 2008
(ix) Differentiation	✗ Not applicable	
(x) Transcendence (end justifies the means)	✓[Rhetorical Strategy 4]	Ware & Linkugel, 1973; Tedeschi & Reiss, 1981; Oliver, 1991; Jameson, 2000; Cheney <i>et al.</i> , 2004; Bebbington <i>et al.</i> , 2008
(xi) Attack accuser	✓[Rhetorical Strategy 8] 'Intimidation/Challenge'	Oliver, 1991; Rosenfeld <i>et al.</i> , 1995; Bolino & Turnley, 2003
(xii) Compensation	✗ Not applicable	See note * above.
4. (xiii) Corrective action	✓[Rhetorical Strategy 1]	Goffman, 1974; Bebbington <i>et al.</i> , 2008
5. (xiv) Mortification	✗ Not applicable	See note * above
<i>Bolino & Turnley's (2003) impression management profiles</i>		
(i) Ingratiation	✓ [Rhetorical Strategy 6]	
(ii) Self-promotion	✓ [Rhetorical Strategy 7]	Rosenfeld <i>et al.</i> , 1995; Bolino & Turnley, 2003; Ogden & Clarke, 2005
(iii) Attribution	✓ [Rhetorical Strategy 5]	Tedeschi & Reiss, 1981; Oliver, 1991; Benoit, 1995; Jameson, 2000; Aerts, 2005; Ogden & Clarke, 2005
(iv) Supplication	✗ Not applicable	See note * above
(v) Intimidation	✓ [Rhetorical Strategy 8]	See attack 3(xi) above

Source: Adapted from Benoit (1995) and other authors cited above.

Source: Adapted from Benoit (1995) and other authors cited above.

disclosures can be reduced by highlighting similarities and differences, and a typology facilitates the making of comparisons. However, disadvantages include the oversimplification of complex issues and, as social constructs (Bailey, 1994), they must be used carefully (Shrives & Brennan, 2015). By their nature, explanations are rhetorically charged. By drawing together a wide range of rhetorical strategies into a new typology, we provide insights into, arguably, the whole purpose of explanations, which is to persuade readers that non-compliance is appropriate/acceptable. In this section, we introduce each of the nine rhetorical strategies in our typology, illustrating each one with examples of corporate governance non-compliance explanations, culminating in the typology itself in the second half of the section.

3.1. Towards a typology of explanations

In this section, examples of explanations illustrating the typology are discussed. The majority of these examples reflect the idea that they are written so that the non-compliance explanation either mimics compliance (isomorphic behavior) or appears even better than compliance (DiMaggio & Powell, 1983; Elsbach & Sutton, 1992) thereby making the company's approach to compliance appear legitimate. Each category within the typology is now discussed in turn.

3.1.1. Corrective action

Corrective action is an effective and convincing rhetorical strategy (Benoit, 1995) if it is utilized in the form of a statement such as 'the problem has been resolved or is to be resolved'. Most problems in life seem less concerning when the promise of restitution is provided. Corrective action is very powerful in mimicking compliance because it implies that compliance is already achieved or about to be achieved. The problem is resolved and the company's approach appears legitimate. However, when used alone, corrective action provides an incomplete picture of compliance because questions remain. Readers need to know why the non-compliance occurred, was any damage caused in the meantime and is it likely to re-occur? If, however, a company genuinely believes it should not comply with the Code and non-compliance with the Code is best for the company, then corrective action is inconsistent with that view. Corrective action acknowledges that an issue exists. Four sub-categories of corrective action are included in our typology: (1a) Corrective action already taken; (1b) Corrective action to be taken (with clear timescales); (1c) The promise of corrective action in the future (without clear timescales); (1d) The promise to keep the need for corrective action under review. In 1d, readers will not know whether the directors disagree with the Code or simply do not feel the need to comply.

In Example 1a, a full and clear explanation is provided by Tesco, in that it includes the Code provision breached, the precise nature of the breach and how the breach was addressed/corrected. If the non-compliance is temporary, (as in Example 1a) that may be seen as an oversight but it may also suggest lack of succession planning. A simple chart detailing which non-executive directors were in place at different times, would have identified this 'gap' (and forward planning would have meant this 'breach' could probably have been avoided). It is not unreasonable to expect this level of planning from a FTSE 100 company. However, the counter argument is that it is possible that some managers would not have disclosed this four-day non-compliance, identifying it as trivial, so Tesco is to be commended on admitting something which possibly not even institutional investors would have noticed.

Example 1a: Corrective action already taken

Provision B.1.2 of the Code requires at least half of the Board, excluding the Chairman, to comprise Non-executive Directors determined by the Board to be independent. Tesco has complied with this provision except for the first four days of the financial year, when it had one more Executive Director than Non-executive Directors (excluding the Chairman). However, following Sir Terry Leahy's retirement and the appointment of Philip Clarke as his successor as CEO in March 2011, there has been at least an equal number of Non-executive and Executive Directors.

Where there is a promise to correct something in the future (Example 1b and Example 1c) and no further information is provided, then again a question remains as to why the non-compliance has occurred. Example 1b is a good example of a clear explanation which is easy to appreciate. Example 1c is arguably not so good because readers are not told why this non-compliance is in the best interests of the shareholders. Keeping the situation under review (Example 1d) is also perhaps a good approach to non-compliance, because it shows an open approach which is consistent with a flexible approach to compliance. Corrective action, or the promise of such, is not by itself a complete explanation of non-compliance. Even if the non-compliance is temporary, readers still need to be informed why it has occurred – was it a lack of succession planning or was it an oversight or did an unexpected event occur? An explanation is *always* required, even if company managers are reluctant to admit to oversights.

Example 1b: Promise of corrective action to be taken (with clear timescales)

In 2011, the Company has complied with the provisions of the UK Code, except for the following:

- B.6.1 Performance evaluation of the Board, its committees and its individual Directors;
- Schedule A of the UK Code recommends share options and awards should not vest in less than three years.

The reason for non-compliance was the short period between the formation of the Group and the year end (B.6.1) and the existence of share option arrangements prior to admission (Schedule A). B.6.1 will be complied with in 2012.

Source: Polymetal plc annual report 2011, p. 75.

Example 1c: Promise of corrective action in the future (without clear timescales)

Succession and board changes

My retirement will take effect at this year's Annual General Meeting on 26 July 2012. At that point, Graham Mackay will take over as Executive Chairman for an interim period of one year and Alan Clark, currently Managing Director of SABMiller Europe, will become an executive director and Chief Operating Officer. At the end of the interim period, the intention is that Graham will become Non-Executive Chairman and that Alan will succeed him as Chief Executive. We acknowledge the recommendation in the UK Corporate Governance Code that a chief executive should not go on to be chairman of the same company and that the roles of chairman and chief executive should not be exercised by the same individual. Nevertheless, after long deliberation, we believe that these appointments are in the best interests of SABMiller and its shareholders. . . .

Job specifications setting out the respective authorities and responsibilities of the Executive Chairman and Chief Operating Officer have been agreed by the board and the directors are confident that Graham and Alan will continue to work effectively together during the transition and thereafter. Any risk of an over-concentration of decision-making powers in one person will be mitigated by the fact that John Manser, our senior independent non-executive director and chairman of the audit committee, will in addition become Deputy Chairman of the board. . . .

It is also the board's intention now to begin the process of recruiting a new independent non-executive director, with the expectation in due course he or she could become the senior independent director in succession to Mr Manser.

Example 1d: Keeping the situation and need for corrective action under review

The Remuneration Committee

During 2011 this Committee comprised independent Non-Executive Directors David Allvey (Chairman), Gavin Darby (resigned May 2011) and Christopher Knight, together with Vanni Treves. With effect from 1 January 2012, the Committee now comprises Christopher Knight (Chairman), Alan Brown and Sir David Reid. The Code requires the Remuneration Committee to have at least three independent Non-Executive Directors whilst allowing the Chairman of the Board of Directors of the Company, if considered independent on appointment, to be a member. Whilst mindful of its non-compliance with the Code, the Board has considered and still believes that the Committee has the necessary skills and expertise required. However, this will be kept under review and steps taken to look at appointing an additional Non-Executive Director during the year.

In relation to the promise of corrective action in the future, instances of unrealized promises were found in explanations. Example 1e demonstrates that, even for large visible corporations, promises of corrective action can remain unfulfilled, such that the rhetoric does not match reality. Readers of explanations need to check whether and when promises of future compliance are realized.

Example 1e: Unrealized promise

The Board

The Chairman, Mr A J Habgood, continued to act in the capacity of Chief Executive until 1 November. The Board recognised the concerns, expressed in a general context, about the possible negative effects of a concentration of power through a combined Chairman and Chief Executive role and, although it believed these did not apply to the Company for a variety of reasons, it was decided at the end of February 2005 that, following the demerger of Filtrona in June 2005, the roles of Chairman and Chief Executive would be separated. Having originally agreed to do so, Mr C P Sander subsequently decided not to assume the position of Chief Executive for personal reasons.

3.1.2. Bolstering

Bolstering refers to some positive event which diverts readers away from the area in question (see [Benoit, 1995](#); [Bebbington, Larrinaga & Moneva, 2008](#)). The diversion to positive issues is particularly successful if the “positive traits or actions appear relevant” ([Benoit, 1995, p. 77](#)). Thus, stating the company had received an award for good corporate governance may make readers less concerned about incidences of non-compliance. The non-compliance is overshadowed by the company appearing good at governance with the company’s approach equivalent to those complying and legitimacy is restored ([Suchman, 1985](#)). Such diversionary tactics would be of particular concern where no explanation for any non-compliance was provided.

Bolstering is illustrated in Example 2. Interestingly, while not complying with what is arguably a cornerstone of the corporate governance code (the proportion of independent non-executive directors), Aggreko claims that its own allegedly superior (bolstered) but invented rule achieves a better result than compliance. This explanation can also be coded to rhetorical strategy 4 (transcendence – see later) because the company is, in effect, saying that following its own rule more than compensates for the non-compliance.

Example 2: Bolstering

The Code states that at least half of the Board, excluding the Chairman, should be independent Non-executive Directors. However, the Directors believe that, beyond a certain size, Boards risk becoming ineffective at control and decision-making; they certainly become more expensive as they grow larger. Ideally, in our view, the Aggreko Board works most effectively, and represents best value for shareholders, with no more than ten people sitting round the table. Applying the “no more than ten round the table” rule leaves nine places for executive and Non-executive Directors.

Although it is understandable that boards can be unwieldy if overly large, no research indicates an optimal number for a large listed company albeit there is some support from [Yermack \(1996\)](#) whose research indicates that market valuation is negatively correlated with board size.

3.1.3. Minimization of negative feelings

Minimization of negative feelings is a common rhetorical strategy discussed in the literature (Bebbington et al., 2008; Goffman, 1959; Schlenker, 1980; Scott & Lyman, 1968; Tedeschi & Reiss, 1981). This type of rhetorical strategy in explanations implies that non-compliance is likely to cause little damage, legitimacy is not threatened and the Code provision not complied with is trivial. It is a key principle of the Code that non-compliant companies need to convince readers in their explanations that they have put in place (an)other mechanism(s) to ensure that the system operated is as good as compliance. If the Code section is treated as unimportant (in Example 3 concerning the percentage of NEDs classified as independent), then the implication is that no other governance mechanism is required. This seems counter to the spirit of the Code. This “minor exception” and Code non-compliance is further discussed in relation to Example 7 further on.

Example 3: Minimization of negative feelings

Throughout 2011, the Group complied fully with the UK Corporate Governance Code 2010 (with the minor exception noted on page 66) and also with the Sarbanes-Oxley Act 2002 (US). The Board values corporate governance highly and this is reflected in our governance principles, policies and practices and our everyday working processes. This approach is backed by continuous improvement based on measurement against internal objectives, external audits and benchmarking and a rigorous approach to risk management.

...

Compliance with the UK Corporate Governance Code 2010 (UK) and the Sarbanes-Oxley Act 2002 (US)

The Group has complied with the provisions of the UK Corporate Governance Code 2010 throughout 2011 with the following minor exception:

B.1.2 Between August 2010 (when John Scarisbrick completed nine years' service as an independent non-executive director) and the appointment of Janice Roberts and Larry Hirst in January 2011, there were four independent non-executive directors and six executive directors. The Group achieved full compliance with the requirements of s404 of the Sarbanes-Oxley Act 2002 for the sixth successive year.

A key aspect of non-executive directors is their independence, a cornerstone of the Code, and yet this provision is the most commonly non-complied with in the UK (Shrives & Brennan, 2015). Can such non-compliance be called “minor” when apparently the board “values corporate governance highly?”

3.1.4. Transcendence

Transcendence alters the context of the action by taking the view that some act is necessary (non-compliance), because of the need to envision a more important worldview (or more simply, ‘see the bigger picture’). The action may *initially* seem bad but in fact has a ‘silver lining’ which more than compensates and thus the ‘end justifies the means’. Employing a consequentialist approach is a common rhetorical strategy discussed in the literature (e.g., Bebbington et al., 2008; Jameson, 2000; Oliver, 1991; Schlenker, 1980; Scott & Lyman, 1968; Tedeschi & Reiss, 1981). In one sense, the bad action is attributed to a good outcome and thus it could be seen as a variant of attribution (Aerts, 2005). Thus, when managers choose not to comply with regulations (or Code) they emphasize the “virtues of non-compliance” (Oliver, 1991, p. 150). The implication is that shareholders can be better served by non-compliance. Similarly, Elsbach and Sutton (1992, p. 699) discuss how companies can use tactics to “shift[ed] attention away from the controversial actions and toward the socially desirable goals”. The explanation in Example 4 suggests the higher goal of the important contribution of the non-independent non-executive directors is more important than Code compliance. However, the explanation does not stand up to scrutiny. While the Code is breached by virtue of length of service, negative feelings for this breach are ameliorated by the statement that the non-executive directors (note that there is more than one who have caused a breach) make an “important contribution” and have “invaluable experience”. It is perfectly natural for boards to want to retain non-executive directors who have proved their worth over the years. The Code does not prevent that happening. However, they cannot then also fulfil their role as an *independent* non-executive. The existing non-executive directors could be classified as grey non-executive directors (i.e. non-executive directors who are not independent). Other independent non-executive directors would then need to be appointed to ensure that important control (the additional pair of independent eyes) is maintained. In Example 4 this does not seem to be the case.

Example 4: Transcendence

Messrs Hemingway, Gray and Gillespie are not regarded by the Board as independent under the Code because they have advised the Company over many years; nor is Mr Park due to his having been chairman of Northcliffe Newspapers within the last five years. Nevertheless, the Board believes that these non-executive Directors make an important contribution to its deliberations and have invaluable experience of the Company, its business and its staff.

3.1.5. Attribution

Attribution involves causal explanations of events that manifest in a tendency to claim more responsibility for successes than for failures. In the literature, attribution is a common rhetorical strategy (e.g., Aerts, 2001; Jameson, 2000; Tedeschi & Reiss, 1981). When challenged, the respondent agrees that there is an issue (hence the company's approach cannot be seen as equivalent to, or better than that specified by the Corporate Governance Code), but the excuse given blames something or someone else (Scott & Lyman, 1968). This internal/external dichotomy is a key defining feature of attribution studies. Attribution can be particularly effective as a rhetorical strategy when combined with another rhetorical strategy such as corrective action. Four sub-categories of attribution are included in our typology: blaming external circumstances (Example 5a), blaming internal factors (e.g., a board restructuring) (Example 5b), non-compliance attributed to a legal contract (typically set up prior to the Code) (Example 5c) and shareholders' votes/consultation led to non-compliance (Example 5d). Example 5a attributes executive contracts exceeding one year, contrary to Code provisions, to "external competitive pressures".

Example 5a: External attribution

Service Contracts

Contracts of service are negotiated on an individual basis as part of the overall remuneration package and their length is inevitably conditioned by external competitive pressures. For this reason, the contracts of some of the executive Directors exceed the one year recommended in the Code.

Example 5b is rather more complex as non-compliance is attributed to an internal event (board changes) and also the determination of efficiency targets set by the water regulator (referred to as "AMP4"), which permitted the company to raise water prices by almost a quarter. The attribution in Example 5b is coded to "internal" because the board changes are referred to first and that seems to be the essence of the continuation of the chairman. The reference to "mm02" in Example 5b is required because the chair is also chair of another FTSE company (contrary to Combined Code (FRC, 2003) provision A.4.3–No individual should be appointed to a second chairmanship (sic) of a FTSE 100 company). Note that it is not at all clear what the non-compliance is and no Code provision is provided (thus this explanation is also coded to rhetorical strategy 9d (no Code provision number provided) discussed at the end of Section 3.1).

Example 5b: Internal attribution

The former Chairman, Mr T D G Arculus, was appointed as chairman of mm02 in July 2004 but was requested by the Board to remain in office until 31 December 2004 to provide some continuity while a number of Board changes took place and also while the AMP4 Final Determination was awaited by Severn Trent Water.

In Example 5c, the non-compliance is attributed to contractual arrangements which came into force before the Code was in its current form. Thus, the company or its management cannot be to blame for this. In the 2010 Corporate Governance Code (FRC, 2010), B.7.1 recommends that all directors of FTSE 350 companies should be subject to annual election by shareholders. International Airlines Group did not comply with this Code provision as is indicated in Example 5c. Note again that no Code provision is provided, so this explanation is also coded to rhetorical strategy 9d.

Example 5c: Attribution to contractual constraints

(v) Annual re-election of Directors:

At the time of the merger, British Airways and Iberia agreed that the re-election of Directors would not be done on an annual basis for an initial period. At an ordinary shareholders' meeting of the Company held in November 2010, all Directors were elected for a four-year period from the merger effective date, January 21, 2011.

Notwithstanding the above, the Board regulations contain a provision which establishes that the following Directors will resign and stand for re-election in accordance with the following calendar, without prejudice to the ability of the shareholders' meeting to remove such persons as a Board member at any moment according to applicable law.

Finally, in Example 5d, the non-compliance is explained by reference to shareholders. The implication is if a wrong decision was taken, then the shareholders played a part by giving their approval.

Example 5d: Attribution to shareholder votes/consultation

Appointment of the Chairman and Chief Executive

The Company acknowledges that the appointment of Sir Bill Gammell from the role of Chief Executive to Non-Executive Chairman of the Board is an exception to the UK Corporate Governance Code. However, in making the appointment the Board agreed unanimously that looking forward this move was in the best interests of the Company and its shareholders. The Board believes that, in making this appointment, the Nomination Committee undertook a robust process. As part of this process, the Company consulted with its major shareholders who indicated their approval of the Board changes.

Non-compliance can be justified to a specific cause so there is no need to attribute the non-compliance to something or someone internally in the company. Thus, as such, there is no legitimacy question. However, when the board “unanimously” claims (see the Cairn Energy plc, Example 5d above) that it was in the best interests of the Company and the shareholders, investors need to be willing to question this as the board may be focussing mainly on its own interests. As a result, we have classified attribution as a rhetorical strategy. Attribution and strategies 6, 7 and 8 can be more effective in affirming legitimacy if they are combined with some of the earlier strategies such as minimisation of negative feelings (see Section 5.2).

3.1.6. Ingratiation

Ingratiation is a rhetorical strategy concerned with flattering others (Bolino & Turnley, 2003; Jones & Pittman, 1982; Ogden & Clarke, 2005; Tedeschi & Melburg, 1984). An example of ingratiation would be the board trying to flatter those who were involved in the development of the Code. To the audience this generates a type of legitimacy, because it implies the management or the board are aligned with the developers of the Code. Two examples, Example 6(i) and Example 6(ii), are provided to illustrate this concept.

Example 6(i): Ingratiation

We fully support the new Code and the direction in which it is taking the practice of corporate governance in the UK and, in particular, the emphasis placed on the board’s responsibility for providing leadership necessary for the long term success of the company.

Example 6(ii): Ingratiation

The non-executive directors of the Company, together with the executive directors and the company secretary, are committed to ensuring that the Board of the Company provides sound and effective leadership. The Corporate governance statement sets out the Company’s compliance with the UK Corporate Governance Code (“the Code”). The Board welcomes the clarity provided by the Code and the added emphasis on responsibility and accountability. However, as the statement about the role of the Board in the Corporate governance statement makes clear, the Board believes that good governance and effective leadership are about more than adherence to the Code or to any particular guidance. The members of the Board take very seriously their responsibilities to promote the success of the Company, whilst managing risk and demonstrating the high ethical standards and behaviours expected of everyone in the Company.

In both cases, despite the ingratiation, neither company fully complies with the Code. In Example 6(i), there are two non-compliances, one to do with the availability of the terms and conditions of appointment of non-executive directors and one concerning the Chair of the board chairing the remuneration committee. In Example 6(ii), it is interesting to explore the wider context. Fees earned by executive directors in respect of non-executive positions are not disclosed (contrary to Code provision D.1.2) because “it is not considered relevant” (Smiths Group plc annual report 2011, p. 70). Smiths Group does not (despite claiming to welcome “clarity”), provide the Code provision reference (thus the explanations elsewhere within its annual report are coded to rhetorical strategy 9d). Code provision D.1.2 requests disclosure of whether the executive directors retain such income and, if so, the amount of the income. This is part of accountability of executive directors and helps shareholders determine the extent of other interests which may divert the executive directors’ attention away from the company in question. Of course, it may not be relevant because the amounts are small but this seems unlikely. Shareholders are likely to assume the amounts involved are significant, yet are undisclosed. This non-disclosure is inconsistent with the company’s ingratiation statement in Example 6(ii) and provides further support as to why we coded this explanation as the rhetorical strategy 6 (ingratiation).

3.1.7. Self-promotion and exemplification

Self-promotion and exemplification are viewed as two separate rhetorical strategies in the literature (Bolino & Turnley, 2003; Jones & Pittman, 1982; Ogden & Clarke, 2005) but for the purposes of this study it would be difficult to reliably distinguish between them. Self-promotion is where individuals or organizations try to promote themselves by claiming a level of competence. This is similar to companies claiming that their behavior is an example to others (exemplification). A hypothetical example of self-promotion and exemplification might read: “Our company has been skilful and rigorous in applying the Code and meeting its objectives” or “The company has won an award for its governance procedures”. The audience is thus directed away from any questioning of governance procedures. In Example 7, despite not complying with the Code, the company claims a strong governance system is in place.

Example 7: Self-promotion and exemplification

The Board values corporate governance highly and this is reflected in our governance principles, policies and practices and everyday working processes. This approach is backed by continuous improvement based on measurement against internal objectives, external audits and benchmarking and a rigorous approach to risk management.

The non-compliance is described as “minor” (in Example 3 earlier). The explanation for non-compliance is provided five pages later (p. 66) comprising a breach of the requirement for a majority independent board (ARM Holdings plc had, for a period of time, four non-executive directors and six executive directors). Others might consider such a breach to be fundamental rather than “minor”. Also, the breach arose when a non-executive director had completed nine years’ service, not exactly a circumstance that was sudden; that could not have been anticipated. Under the Code, terms beyond six years should be treated to a particularly rigorous review. Non-compliance is certainly consistent with a strong governance system but the self-promotion rhetoric on page 61 of ARM Holdings plc’s annual report (Example 7) appears to be inconsistent with the explanation on page 66. It is this inconsistency that the audience needs to become aware of because it raises questions about the legitimacy of the explanation and hence the company’s corporate governance system.

3.1.8. Intimidation/challenge

When writing about defiance, Oliver (1991) identifies the strategies of challenge and attack. Challenge could be where companies challenge the basic premise of the Code or individual principles or individual Code provisions. In contrast, attack would be more aggressive and may involve belittling or denouncing the Code. Challenge might be particularly powerful as a rhetorical strategy when combined with transcendence (“ends justify the means” – rhetorical strategy 4). In that way, any “negative repercussions” of non-compliance can be removed by references to “higher goals” (Aerts, 2005, p. 497). When the Code is challenged, then the implication is that non-compliance cannot threaten legitimacy and governance can be, in fact, improved (Elsbach & Sutton, 1992). In this instance, the management is changing the direction of questioning away from the company to the Code and it is the Code’s legitimacy that is being questioned. Our typology includes two sub-categories: 8a – slight challenge and 8b – more aggressive or determined challenge. Example 8a appears to be an attack on the Code: “divisive” to the board and “disruptive” to the chairman are part of the attack. This explanation could have been classified as 8b – a more aggressive or determined challenge – as it is quite a strong attack. However, it was classified as 8a because of the moderating word “potentially” in Example 8a. Example 8b forms a useful comparison. Although outside the sample of this study (it is a FTSE 250 company), the directors of this company have criticized the Code for a number of years. The board’s explanation as to why it does not agree with current thinking on governance, while strongly worded, demonstrates the importance of flexibility in relation to compliance. Interestingly, the directors believe that the views of employees and customers are more valuable than institutional investors. This critical approach is useful in that it questions some underlying assumptions of the Code. The audience needs to decide whether the attack is indeed genuine or simply a convenient excuse for non-compliance. If the governance advocated by the board or management does not appear to be of equal stature to that required by the Code then, arguably, the latter is the case.

Example 8a: Slight challenge

The Board has not, as required by the Code, identified a senior independent non-executive Director since it believes that to identify such an individual is potentially divisive to a unitary body, as the Board is, and disruptive to the role of the Chairman.

Example 8b: More aggressive or determined challenge**Corporate governance**

In last year's statement, the view was advanced that many aspects of current corporate governance advice, as laid out in the Combined Code, were "deeply flawed". The statement pointed out that "compliant pub companies had often fared disastrously in comparison with non-compliant ones. In particular, pub companies in which the CEO became chairman and which had a majority of executives . . . usually with previous experience of the pub trade, avoided making catastrophic errors to which compliant companies seem prone". It was also pointed out that setting targets for bonuses had also often backfired, encouraging companies to take reckless decisions in order to enhance earnings.

Last year's statement was particularly critical of the Code itself, which placed a huge emphasis on meetings between directors and shareholders and placed almost no emphasis on directors taking account of the views of customers and employees which are far more important, in practice, to the future well-being of any company.

3.1.9. Concealment or denial

Not all companies are quite so upfront about their view of the Code. Concealment is concerned with hiding or disguising non-conformity. Denial implies the event of non-compliance did not occur (Schonbach, 1980) or that managers claim to be innocent of the event (Schlenker, 1980). This can make non-compliance appear to mimic compliance. In the context of non-compliance explanations, there are a number of possibilities. Companies could claim compliance despite not complying or admit to some non-compliance without disclosing all non-compliance. In this study, non-compliance not explained/ omission of explanations would be difficult to identify without undertaking an audit of the business (although this remains an important area for further work). Four concealment rhetorical strategies are included in our typology:

- Non-compliance stated but no reason/explanation given (rhetorical strategy 9a). This also applies where the company states that the issue is now resolved but does not provide *any* explanation as to why the issue occurred in the first instance. If readers have to ask further questions, then the explanation is not fully articulated. Readers may not even appreciate that it is non-compliance that is being described. Because no explanation is provided, it may be indistinguishable from compliance, especially where readers do not have detailed knowledge of the Code.
- Companies (i.e., the managers that write the reports) may try to disguise non-compliance through the use of 'weasel words' (words or statements that are intentionally misleading) (rhetorical strategy 9b). 'Weasel words' are difficult to identify *ex ante* as they are likely to vary from company to company, each using them in a different way. In our study, these are words which distract readers from non-compliance, instead focusing on compliance. For example, companies may claim 'full compliance except for' certain items: the company may refer to three items of non-compliance but lists four, perhaps combining two together. The company may claim 'highest' standards of corporate governance despite non-compliance. Although it is acceptable to claim high standards and not comply with all aspects of the Code, 'highest' seems too bold a claim. The use of 'weasel words' can mean that readers are distracted or misled and either believe the company is complying or are simply unsure as to whether the company is complying or not.
- Managers may employ a disclosure strategy where non-compliance explanations have to be searched for (structural rhetoric). We call this 'hunt the thimble' (rhetorical strategy 9c). In this rhetorical strategy, compliance is often claimed with the proviso: 'except as noted below', with the word 'below' being undefined, typically referring to the pages following (i.e., non-compliances are not bulleted, numbered or listed immediately below). This is problematic for a number of reasons. At times, it can be difficult to distinguish between the description and claim of compliance, and the explanation of non-compliance. Non-compliance can seem like compliance. In addition, readers do not know how many instances of non-compliance to look for, although the presumption would be at least one. Finally, it can involve reading through a large number of pages because the end point is unspecified. Thus, non-compliance is hard for readers to find and the company is not being completely transparent.
- The last rhetorical strategy (9d) relates to whether or not companies provide the Code provision number relating to the area of non-compliance. Surprisingly, Code provision section identifiers are commonly omitted from explanations, making it difficult for readers to be sure what exactly is not being complied with. Omitting the Code provision number is not transparent concerning exactly what is not being complied with (references such as 'A.3.2' very clearly highlight issues in the text and are easy for the eye to pick out).

In Example 9a (i), although "page 49" does provide some more information, it is not clear exactly why one non-independent board member had to be on the remuneration committee. Readers have to identify the members of the committee and then read all the directors' details to work out which non-executive director is not independent and then make an assumption as to why one of them had to be on the committee. Thus, the reason for the non-compliance is not provided, thereby requiring further work by readers.

Example 9a (i): Non-compliance stated but no reason given

During the year the Company did not comply with the following provisions of the UK Corporate governance code:
(i) Independent membership of the Remuneration Committee: one member of the committee is not independent.
Refer to the Report of the Remuneration Committee on page 49;

Similarly, in Example 9a (ii), readers are informed that one non-executive director could not attend the AGM due to “another pressing business commitment”. Although some may see this as an explanation, it raises a number of issues. What precisely was the reason for AGM non-attendance? Can this person devote sufficient time to being a non-executive director? GSK could have provided information to answer these questions. Earlier in its annual report, GSK talks of welcoming the introduction of the Code and complying with a new provision “ahead of time” (p. 82) but it is difficult to marry these voluntary disclosures with an explanation that is not an adequate explanation.

Example 9a (ii): Non-compliance stated but no reason given

Throughout 2011, we complied with the provisions of the Code, except that Larry Culp was unable to attend the AGM due to another pressing business commitment.

In Example 9b, the phrase “the Group complied with all of the provisions” contradicts the subsequent phrase “with the exception of”, particularly where a key aspect of the Code was not complied with and is arguably misleading. The explanation appears to be crafted to read like full compliance.

Example 9b: Use of ‘weasel words’

Putting governance into practice

We support the UK Corporate Governance Code published by the Financial Reporting Council in June 2010 (the “Code”). We consider that the Group complied with all of the provisions of the Code throughout the year ended 31 December 2011 with the exception of the Code provision that at least half of the Board, excluding the Chairman, should be independent Non-executive Directors; the reasons for this are explained in detail in the paragraph below entitled “Non-executive Directors”. Copies of the Code are publicly available at www.frc.org.uk.

The next examples relate to ‘hunt the thimble’ disclosure. In Example 9c (i), “below” means a large block of text which readers must hunt through as if looking for a thimble or a ‘needle in a haystack’. In place of the word “below”, Example 9c (ii) uses the imprecise phrase “save where otherwise identified”. The scattered nature of the disclosure makes it difficult to identify all the non-compliances and find the non-compliance explanations.

Example 9c (i): ‘Hunt the thimble’ disclosure

Corporate Governance

The group is committed to the highest standards of corporate governance. During 2003, the board reviewed its governance arrangements in the light of the new Combined Code on Corporate Governance (the Code) and the Guidance on Audit Committees (the Smith Report) and made changes as necessary and appropriate at the time. Although the company did not fully comply with all the provisions of the Code throughout 2004, further governance changes were approved by the board in the year that will ensure full compliance throughout 2005 and beyond. The changes made in 2004 and details of non-compliance during the year are explained below together with a report on how the principles of the Code were applied.

Example 9 (ii): Hunt the thimble disclosure

The Board is accountable to shareholders for good business governance. The way in which Hanson applies the principles set out in the Combined Code on Corporate Governance issued by the Financial Reporting Council in July 2003 (the “Code”) is described within this Report of the Directors and in the Remuneration report. Hanson has been in full compliance with this Code throughout the year under review, save where otherwise identified.

Table 3

Extent of non-compliance.

Panel A: Unit of analysis: Companies	FTSE 100 Companies			
	2004/05		2011/12	
No. non-compliance items	No.	%	No.	%
1	21	33%	25	58%
2	16	25%	10	23%
3	15	24%	2	5%
4	6	10%	4	9%
5	0	0%	2	5%
6 or more	5	8%	0	0%
Total number of non-compliant companies	63	100%	43	100%
Total number non-compliance items	168		77	
Average	2.67 breaches		1.79 breaches	
Panel B: Unit of analysis: Explanations				
Total explanations of non-compliance ^a	146	100%	71	100%
Average per non-compliant company	2.32 explanations		1.65 explanations	

^a This is lower than the number of Code items breached (168/77) as some Code breaches are combined into one explanation. Source: [Shrives and Brennan \(2015\)](#).

A variant of 'hunt the thimble' is 'upstairs/downstairs' disclosures. This is where the compliance statement appears in the middle of the corporate governance report with explanations for some Code breaches above and some below. The overall effect is confusing for readers. Consider, for example, Example 9c (iii). At first glance, the compliance statement appears at the end of the corporate governance report and refers to two items of non-compliance. However, the phrase "unless otherwise stated above" suggests there are other instances of non-compliance not explained in the compliance statement. Example 9c (iii) has elements of 'hunt the thimble', but is better than those statements where readers have no guidance at all as to where to look for explanations. In this case of rhetorical manipulation, two items are provided after the phrase "further exceptions" (not quoted here for brevity). However, readers are not directed to those items "stated above" and effectively they remain hidden. This approach to disclosure is quite unhelpful to readers.

Example 9c (iii): 'Upstairs/downstairs' disclosure

Compliance with the Code Provisions

Unless otherwise stated above, the Company has complied with the provisions of the Code throughout the accounting period under review with the following further exceptions.

Finally, one of the most common areas of non-disclosure relates to the situation where the Code provision number (for example A.3.2) is excluded. [Shrives and Brennan \(2015\)](#) include this as an aspect of disclosure quality. There are various reasons why companies may omit Code provision numbers (because the Code provision numbers change, or managers are not sure which is the correct Code provision number, or two Code provisions cover similar aspects) but it is also an effective rhetorical strategy. Identifying the Code provision number invariably draws attention to non-compliance, particularly when there are a number of non-compliances. Eyes tend to be drawn to section identifiers such as C.3.2 and A.3.1. Thus, not including the Code provision information hides the non-compliance from all but discerning readers. Readers may not know how many Code items are, in fact, being referred to. As evidence for this, web designers advise writers to write (for example) 23 as a number rather than write 'twenty-three' in order to draw attention ([Nielsen, 2007](#)). Example 9d is an explanation with no Code provision.

Example 9d: No Code provision provided

The board considers that it has complied with the principles and provisions of the UK Corporate Governance Code throughout the year with the single exception of the appointment of a senior independent director for the full period under review. As you may be aware, the membership of the board had changed significantly and, until the board had worked together for a period of time, a decision on the appointment of a senior independent director was felt not to be appropriate.

3.2. Typology

Our discussion and examples are drawn together in the form of a typology of rhetorical strategies to justify/persuade/convince audiences of corporate explanations for non-compliance with the UK Corporate Governance Code (Fig. 1). The typology helps readers understand the different approaches that companies take to convince readers of the legitimacy of their explanations. When rhetorical devices are noticed by readers, they are put upon enquiry to be more circumspect as to validity (or otherwise) of the explanation. Explanations should be such that readers are convinced that the company's system of governance is equivalent to that proposed by the Code. We apply our typology as an analytical framework in analysing the non-compliance explanations. The typology is discussed further in Section 4 in connection with coding the data.

4. Issues for research, sample and method

We apply our typology to address three research questions (RQ): What rhetorical strategies do companies use in explanations? (RQ 1); How do the use of rhetorical strategies in explanations compare over two time periods? (RQ 2); and To what extent are rhetorical strategies used in combination? (RQ 3).

The sample comprises two groups of FTSE 100 companies. The first group is made up of FTSE 100 companies whose annual reports relate to the first time compliance with the 2003 Code (FRC, 2003) (typically, year ends 2004 or 2005). The year after the 2003 Code (which contained the most Code changes) was selected. Although the Code has gone through other incarnations, the 2003 changes were most significant and thus it was felt they would provide a variety of explanations to apply the typology. The second group relates to FTSE 100 companies whose annual reports were published in 2011 or

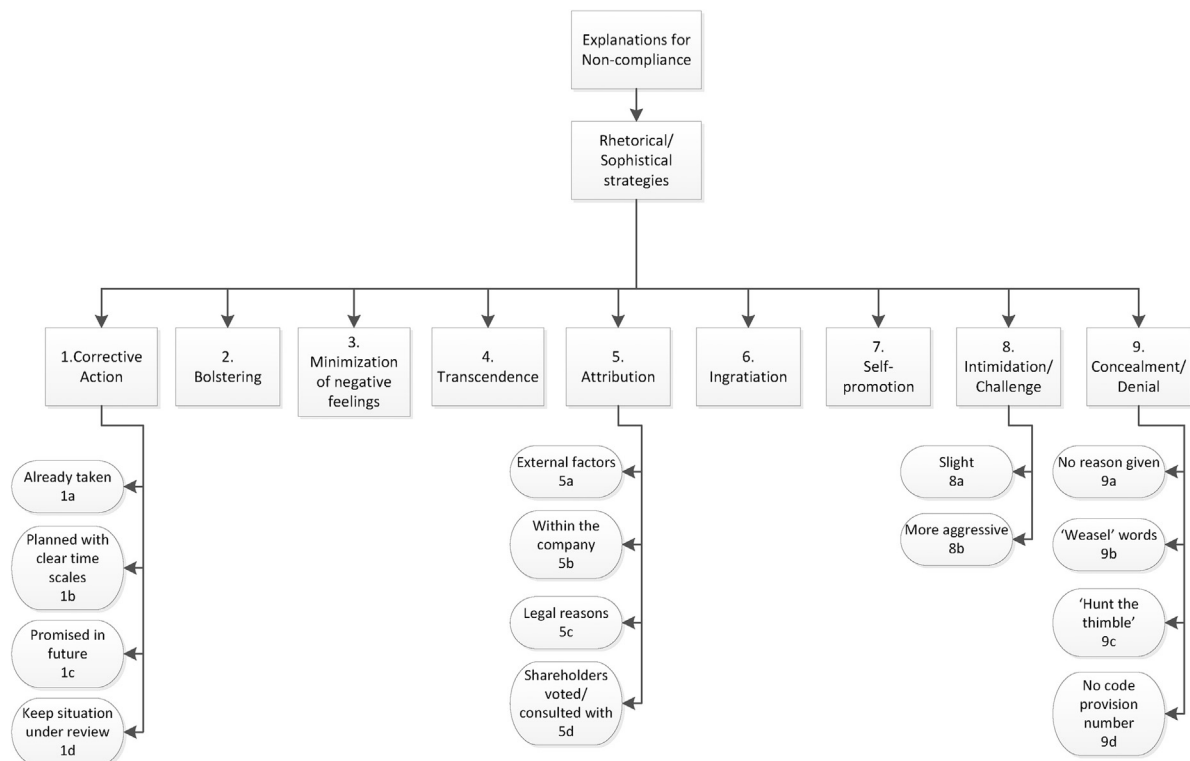


Fig. 1. Typology of rhetorical/sophistical strategies in corporate governance non-compliance explanations (Styled on Figs. 1 and 2 from Beattie, McLInnes, & Fearnley 2004).

Illustration 1

Coding different rhetorical strategies in an explanation.

Extract from International Airlines Group Annual Report and Accounts 2011, p. 40

(Keywords influencing coding decision underlined)

(iv) Appointment of Senior Independent Director:

The Board considered it to be in the best interest of the Company¹ to attribute the functions of the Senior Independent Director pursuant to the UK Corporate Governance Code to the Deputy Chairman of the Board.Throughout the reporting year, Sir Martin Broughton had all the responsibilities and duties of a Senior Independent Director; he was Senior Independent Director in all but name.² On February 28, 2012, the Company formally appointed Sir Martin Broughton to the role.³ Sir Martin Broughton was available to meet major shareholders during the reporting period⁴ but no such meetings took place.

Key: Rhetorical strategy

¹= Rhetorical strategy 4 Transcendence.²= Rhetorical strategy 3 Minimization of negative feelings.³= Rhetorical strategy 1a Corrective action already taken.⁴= Rhetorical strategy 3 Minimization of negative feelings.

Note also that International Airlines Group in this and other explanations did not identify the Code provision breached (rhetorical strategy 9d – no Code provision number provided). International Airlines Group was formed by the merger of British Airways and Iberia and has its headquarters in London.

2012 and relates to the 2010 version of the Code (FRC, 2010), which followed the 2008 global financial crisis and introduced further changes.⁶

Where companies failed to comply with the Code, explanations for non-compliance were extracted from their annual reports. Annual reports were obtained from company websites (preferred), from third party websites or, as a last resort, hard copies were obtained from the company, libraries or other sources. All companies that claimed compliance with the Code were excluded from the sample.⁷ We excluded investment trusts (consistent with MacNeil & Li, 2006) due to their specialist nature and because they are permitted to follow alternative codes, such as the Association of Investment Companies' Code (The Association of Investment Companies, 2016).

The final sample (2004/05 with 2011/12 in brackets) comprised 63 (43) non-compliant companies covering 168 (77) Code breaches (see Table 3). The average number of Code breaches per non-compliant company was 2.67 (1.79). Explanations were identified by searching (electronically) for the words 'compliance', 'Code' or 'corporate governance' within annual reports until the relevant section was found and then repeatedly until the researcher was sure all relevant items were located. Occasionally, explanations were located in different places to breaches so repeated searching helped identify them. A total of 217 (146 in 2004/05 and 71 in 2011/12) explanations were obtained (see Table 3).

This research focuses on the words in non-compliance statements. 'Meaning-orientated' (Smith & Taffler, 2000) content analysis is applied whereby words and meaning are analysed by reference to their co-text (i.e., surrounding text). Meaning-oriented content analysis is an accepted approach in the literature for analysing rhetoric in corporate reports (e.g., Boiral, 2013; Bujaki & McConomy, 2012; Kamla & Rammal, 2013). In analysing rhetoric, the surrounding text needs to be carefully read and interpreted. Once explanations were extracted from the annual reports, a detailed process of coding, re-coding and then second coding was undertaken. The coding categories were based on the nine rhetorical strategies in our typology (see Fig. 1). A coding sheet was developed.⁸ Coding was recorded using keywords to guide the coding as shown in Illustration 1. Coding is an iterative process involving a 'to-ing and fro-ing' approach. The process involved one first coder (the first named author) and two second coders. The first coder devised the coding system, recoded it one month later using a pilot study of 20 companies and then discussed it with the second coders. This method of re-coding enabled the researchers to see exactly how text had been coded and, if necessary, make appropriate amendments to the coding process.

The two second coders were experienced in coding and their purpose was to test the suitability/accuracy of the coding by the first coder. They each coded separate samples (20 items) of the data. The first coder met with both coders separately to discuss coding (this was the training phase) and to demonstrate the range of possible codes. Discussions were held and once agreement was reached then a sample of coding was carried out (as if it was a test). After the 'test' agreement calculations, disputed items were revisited and discussed. Where differences were raised and where it was agreed that an amendment to the coding was needed, the first coder (who coded all the data) went back to revisit items previously coded. If there was some

⁶ The changes in the 2010 Code were substantial and included new principles on the composition and selection of the board including an acknowledgement of the benefits of diversity (to avoid 'groupthink'), new principles on leadership and the time commitment expected of directors. Development reviews with each director (to be carried out by the chair) were also introduced, together with evaluation reviews of the board (which were to be external every three years). All directors were also required to be re-elected annually and non-executive directors were reminded of their responsibility to provide 'constructive challenge'. Finally, the 2010 Code required the company's business model, its link to the risks faced as a result of that model, together with the alignment to performance related pay, to be disclosed (FRC, 2010).

⁷ It is possible companies claimed compliance falsely (which we refer to earlier as the rhetoric of silence). We do not test this. To claim that a breach of the Code did not occur when accused of it, is an example of an image-protection approach (see for example, Ware & Linkugel, 1973). The only example identified during this study of that particular type of denial was from Liberty International's 2004 annual report which stated, "The board considers that Mr Rapp is fully independent . . . As noted above, some external commentators have expressed the opinion that Mr Rapp is not independent" (pp. 58–59). Liberty seems anxious to claim independence for Mr Rapp because he is on both remuneration and audit committees, but he exceeded the nine-year guidance on independence, beyond which annual re-election was required (2003 Code provisions A.3.1 and A.7.2).

⁸ The coding sheet is available from the authors on request.

doubt, the coding rules were then changed to clarify/address the issue raised. If the coder was in doubt as to whether an item should be coded, a rule was established: 'if in doubt do not code'. Calculations of agreement were carried out allowing for the possibility that chance agreement may be a factor (Stemler, 2001). Where coders disagreed, a discussion was always held and, where appropriate, amendments made to the coding system. If the first coder was considered incorrect, corrections were made and similar items were re-coded. This ensured that rigorous standards of content analysis were followed. In each case, at least 20 items were second coded. Using Cohen's Kappa (which adjusts for agreement by chance), the percentage of agreement was 72% for the 2004/05 sample and 83% for the 2011/12 sample. This accords with an agreement strength of 'substantial' (in excess of 70%) and 'almost perfect' (in excess of 80%) (Stemler, 2001).

5. Results and discussion

Table 3 shows the number of companies which failed to comply with the Code. Using a chi-square test, there is a significant difference at the 1% level between compliance over the two time periods ($p = 0.003$) with a significant increase in compliance in 2011/12. The key (top five) areas of non-compliance are summarized in Table 4. Those areas of non-compliance are consistent from one period to the next (2004/5 versus 2011/12) and there is no significant difference between them ($p = 0.551$).

While the system is described as 'comply-or-explain', the numbers complying with the Code have increased over the time period examined. Similarly, of those that do not comply (the focus of this study), companies are now 'not complying' with fewer items and the average number of non-compliances per company has fallen from 2.67 to 1.79 over the period. Table 3 shows a significant difference ($p < 0.05$) in the frequency of non-compliance (other research in Shrides & Brennan, 2015 shows the same pattern for FTSE 250 companies as well as the total FTSE 350). For example, in 2011/12 more companies have just one non-compliance in 2011/12 versus 2004/5 (58% versus 33%) and fewer companies have three or more non-compliance items (18% versus 42%). Thus, it appears that the key company response to date concerns the 'comply' side. As indicated in Table 4, the key areas of non-compliance represent the proportion of the board comprising independent non-executive directors, followed by the composition of the various board committees not complying with the Code. The split of the most common areas of non-compliance are not significantly different between the two periods (using a chi-square test $p = 0.551$). Despite the move to compliance, it remains surprising how many large companies do not comply with what are, arguably, the basic principles of corporate governance.

5.1. Rhetorical strategies used in explanations (RQs 1 and 2)

Rhetorical strategies for both periods are summarized in Table 5. The relative popularity of certain rhetorical strategies is similar in both accounting periods (the top-five ranking is identical). The most popular rhetorical strategies used include minimization of negative feelings (rhetorical strategy 3), the use of 'weasel words' (rhetorical strategy 9b) and transcendence ('ends justify the means') (rhetorical strategy 4). Relative to the frequency of non-compliance, rhetorical strategies are more common in the 2011/12 period: 2004/05: 265 rhetorical strategies – 168 non-compliances (ratio 1.58:1); 2011/12: 197 rhetorical strategies – 77 non-compliances (ratio 2.56:1) (see Tables 3, 4 and 5). Table 5 compares both the number of rhetorical strategies per non-compliance (termed 'breach' for brevity in the tables) and the relative change in this figure over the two time periods. The percentage share of each rhetorical strategy is shown. Trends indicate that managers are making more use of these rhetorical strategies in non-compliance explanations. The relative use of rhetorical strategy 3 (minimization of negative feelings) has increased by 100% and in 2011/12 this rhetorical strategy represents nearly a quarter

Table 4

Breaches by Corporate Governance Code reference: Most common breaches by FTSE 100 companies (ranked by 'top five' breaches from 2011/12).

Code provision 2003/2010 (where different)	Code Details	Breaches 2004/05			Breaches 2011/12		
		No.	%	Rank	No.	%	Rank
A.3.2/B.1.2	At least 50% of the board to comprise independent non-executive directors	23	14%	2	14	18%	1
B.2.1/D.2.1	Remuneration committee constitution	22	13%	3	12	16%	2
C.3.1	Audit committee constitution	30	18%	1	10	13%	3
A.3.3/A.4.1	Guidance re senior independent director	6	4%	Outside top 5	5	7%	4=
A.2.2/A.3.1	Appointment criteria for chair	4	2%	Outside top 5	5	7%	4=
A.4.1/B.2.1	Nomination committee constitution	14	8%	4	4	5%	Outside top 5
A.2.1	Duality principle	9	5%	5	3	4%	Outside top 5
Other breaches		60	36%		24	30%	
Total Code breaches		168	100%		77	100%	

Source: Shrides and Brennan (2015).

Table 5

Incidence of rhetorical strategies in FTSE 100 companies (ranked by 'top five' rhetorical strategies in 2011/12).

Rhetorical strategy	2004/05 (RQ 1)				2011/12 (RQ 1)				Comparison (relates to No. per breach) (RQ 2)	
	Number (No. per breach ^{Note1})	%	Ranking (top 5)	Number (No. per breach ^{Note1})	%	Ranking (top 5)				
3	Minimization of negative feelings	51	(0.304)	19%	1	47	(0.610)	24%	1	+100%
9b	Weasel words	41	(0.244)	16%	3	39	(0.506)	20%	2	+107%
4	Transcendence	38	(0.226)	14%	4	34	(0.442)	17%	3	+96%
1a	Corrective action taken	50	(0.298)	19%	1	15	(0.195)	8%	4	–35%
9a	No clear explanation/ reason given	16	(0.095)	6%	5	13	(0.169)	7%	5	+78%
5b	Attribution – internal	16	(0.095)	6%		3	(0.039)	2%		–59%
5c	Attribution – legal	5	(0.030)	2%		6	(0.078)	3%		+160%
1c	Promise of corrective action in the future (no timescales)	15	(0.089)	6%		12	(0.156)	6%		+75%
1b	Corrective action to be taken with clear timescales	13	(0.077)	5%		6	(0.078)	3%		+1%
8a	Intimidation/challenge – slight	5	(0.030)	2%		1	(0.013)	0%		^–57%
5a	Attribution – external	2	(0.012)	1%		0		0%		^–100%
5d	Attribution – shareholders	2	(0.012)	1%		3	(0.039)	1%		^+225%
7	Self-promotion	1	(0.006)	0%		7	(0.091)	4%		^+1417%
2	Bolstering	3	(0.018)	1%		4	(0.052)	2%		^+189%
6	Ingratiation	0		0%		4	(0.052)	2%		^ increase from zero
8b	Intimidation/challenge – more aggressive	1	(0.006)	0%		0		0%		^–100%
1d	Keep situation under review	6	(0.036)	2%		3	(0.039)	1%		+8%
Total strategies (excluding 9c and 9d shown separately ^{Note2})		265	(1.577)	100%		197	(2.558)	100%		+62%
9c	'Hunt the thimble'	6 cases (10%)				5 cases (12%)				+20%
9d	'Incomplete: No Code provision reference provided'	38 cases (60%)				16 cases (38%)				–37%

Notes: Note 1: Calculated as #/total strategies, e.g., 51/265 = 19%; 47/197 = 24%. Note 2: Rhetorical strategies 9c and 9d can only occur once for each non-compliant company so they are shown separately in this table. The percentage figures for these rhetorical strategies are in relation to the numbers of non-compliant companies (63 and 43 respectively see Table 3). A full list of rhetorical strategies is provided in Fig. 1. Note 3: The symbol ^ in the two right-hand columns of the Table Indicates small numbers in relation to the comparatives.

of the total rhetorical strategies (up from 19%). If areas of non-compliance were inconsequential then this might be understandable but, as Table 4 indicates, the most common non-compliances relate to numbers of independent non-executive directors and the constitution of board committees – all thought to be essential to good governance. Calculated in a similar way, the use of 'weasel words' (rhetorical strategy 9b) has increased by 107% and now represents a fifth of all strategies (up from 16%) while transcendence (rhetorical strategy 4) has increased by 96% and now represents 17% of all rhetorical strategies (up from 14%). It is understandable that transcendence has increased as companies can find it difficult to replace non-executive directors (Whitehead, 2013) and may be reluctant to terminate contracts with experienced non-executive directors who understand the workings of the business. Nevertheless, these companies could consider classifying those people as 'grey' (non-independent) non-executive directors. Increase in the relative use of 'weasel words' is understandable because, as more companies comply, there is a tendency for the remaining companies to construct their explanations to look like compliance. Clearly, users need to be alert to this type of rhetorical strategy. The increasing use of this rhetorical device suggests that companies are under increasing institutional pressures to provide an explanation as to why they do not comply with the Code. Compliance is seen as the default position (unfairly so because that is against the underlying philosophy of the 'comply-or-explain' system) but readers need to be circumspect about the validity of these explanations. Explanations may at first glance appear legitimate but they may not stand up to scrutiny.

No-reason-given explanation (rhetorical strategy 9a) now represents 7% of all rhetorical strategies (up from 6%) and relatively has increased by 78%. This finding is surprising in the light of the emphasis the FRC has placed on better explanations. Companies that do not provide clear explanations are jeopardising the flexible system whereby non-

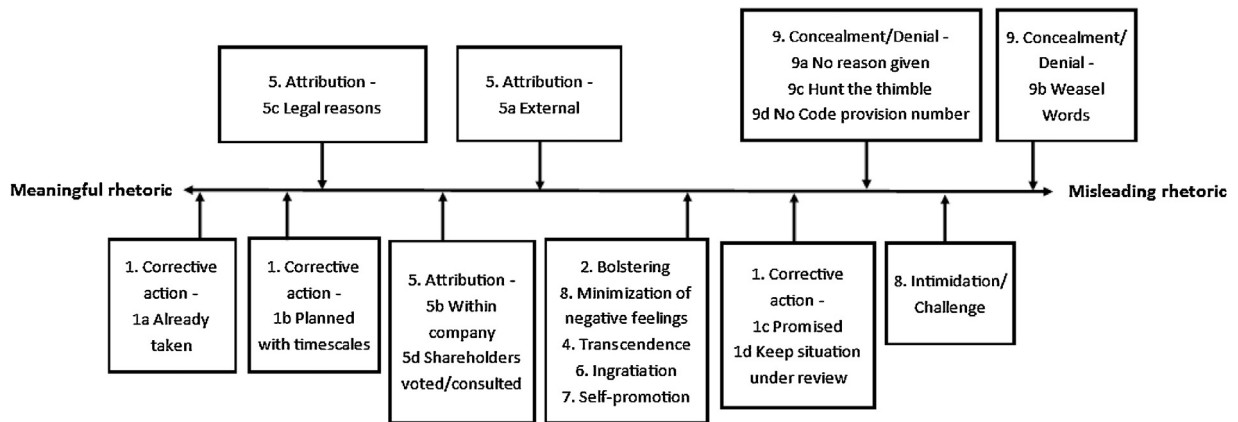


Fig. 2. Continuum classifying rhetorical/sophistical strategies from meaningful to misleading.

compliance with a good explanation is deemed equivalent to compliance. It is perhaps to be expected that corrective action as a rhetorical strategy has fallen relatively by 35% as compliance has increased and companies intending to comply have had more time to comply.

The improvement in explanations accompanied by Code provision references (e.g., A.3.2) (2004/05: 60% of explanations without the Code provision; 2011/12: 38%) may be due to more recent FRC interventions. However, it is still of concern that nearly 40% of companies do not provide the Code provision in their explanations. Companies may not disclose Code provision section identifiers because they are confused about changes in the Code and what particular Code provision applies, or because putting codes in text can draw attention to the non-compliance. While this is understandable, it results in a lack of clarity when explaining non-compliance.

The comparison over the two time periods relates to relatively small numbers and so percentages can be misleading. For instance, attribution for legal reasons (rhetorical strategy 5c) has also increased noticeably, but the numbers are small. This often relates to the requirement in the 2010 Code (FRC, 2010) whereby directors were required to stand for reappointment annually which, in certain cases, was contrary to contracts already in place. Bolstering (rhetorical strategy 2) and self-promotion (rhetorical strategy 7), which are quite similar rhetorical strategies, were rarely used in 2004/05 (just four incidences in total); usage increased to 11 (in total) in 2011/12. Companies appear more likely to present their good aspects than was previously the case. These particular rhetorical strategies are possibly more effective when employed with other rhetorical strategies such as transcendence (rhetorical strategy 4) and this is discussed in the next section.

In order to draw some conclusions from the analysis, in Fig. 2 we present our rhetorical strategies on a continuum from meaningful to misleading rhetoric. We have based our positioning of the rhetorical strategies on whether they are (i) substantive and convincing, (ii) vague and related to impression management or (iii) relate more to misrepresenting the non-compliance or confusing readers. We acknowledge that our positioning of rhetorical strategies on the continuum is subjective. Positioning on the continuum depends on the circumstances and the context. Identification of rhetorical strategies warns readers to be on alert but it cannot, by itself, tell readers what is right and wrong with the company's governance position.

5.2. Rhetorical strategies used in combination (RQ 3)

This study shows that companies make considerable use of rhetorical strategies. From a preparer's perspective, these rhetorical strategies can be particularly powerful when they are used together. This means that readers have to be particularly circumspect when this appears to occur. Ware and Linkugel (1973) and Benoit (1995) discuss strategies which can be used in combination. "[A]s long as multiple strategies do not appear inconsistent – use of multiple image restoration strategies is probably a wise choice . . . [It] may be beneficial in that they reinforce one another". (Benoit, 1995, p. 157). For example, rhetorical strategy 3 (minimization of negative feelings) and rhetorical strategy 1 (corrective action) work quite well together in that the overall message implies that there is little damage and it is now fixed (rhetorical strategy 1a) or will be fixed in the future (rhetorical strategies 1b or 1c). In Example 10, the combination of the two rhetorical strategies is effective as readers are able to map out what has happened, note that it is fixed (rhetorical strategy 1a) and see that there has been little or no damage in the meantime (rhetorical strategy 3).

Example 10: Corrective action completed (1a) and Minimization of negative feelings (3).

Throughout the financial year ended 31 December 2011, GKN was in compliance with the relevant provisions set out in the Code with the exception of Provision B.1.2 which requires that at least half the Board, excluding the Chairman,

should comprise independent non-executive Directors. As stated in the 2010 annual report, a recruitment process was started in late 2010 to identify a replacement non-executive Director following the retirement of Helmut Mamsch on 31 October 2010. From this date until the appointment of Tufan Erginbilgic on 9 May 2011, the board comprised five executive Directors and four non-executive Directors (excluding the Chairman). Since this date, the company had been in compliance with provision B.1.2 and currently comprises four executive Directors and five independent non-executive directors (excluding the Chairman). The Board is content that the independent judgement of the non-executive directors was not adversely impacted during the period of non-compliance.

It is interesting to consider to what extent the use of these rhetorical strategies together might reinforce rhetorical power. One perspective might question why the period of non-compliance occurred at all. The last sentence in Example 10 shows that the company has considered the period of non-compliance and believes independence was upheld. In particular, there are more independent non-executive directors after the corrective action has occurred than executive directors, so this means there is now an element of 'reserve' for future eventualities.

In contrast, rhetorical strategy 4 (transcendence) and rhetorical strategy 1 (corrective action) seem inconsistent because one emphasizes breaching the Code for a good reason and the other is about fixing the breach. However, under certain circumstances, they can be consistent if the breach is for a limited period of time. In Example 11(i), readers are likely to be impressed by Olga Pokrovskaya's credentials but also that the issue with the Code is now *fixed* by Sir Michael Peat's appointment. This explanation is much better than one which just says the problem is now resolved, but provides no explanation as to the solution in the meantime. Code provision C.3.1 requires audit committee members to be independent non-executive directors. It is therefore not very clear why Example 11(i) claims compliance with provision C.3.1 when one of its members does not meet the independence criteria of the Code. This could be down to interpretation of the Code. Perhaps the board believes it has the three independent members required plus an additional (albeit non-independent) member. Interestingly in the following years (up to annual report 2015, [Financial Reporting Council, 2015](#)) the explanation is different in that the board seems to have changed its mind and admits *non-compliance* (see Example 11(ii) which refers to 2013). This illustrates one of the problems of interpreting the Code.

Example 11(i): Transcendence (4) and Corrective action already taken (1a)

Contrary to provision C.3.1 of the UK Corporate Governance Code, only two of the three members of the Audit Committee were independent non-executive directors during 2011. Olga Pokrovskaya is a member of the Audit Committee, but does not meet the independence criteria set out in the UK Corporate Governance Code. Since more than 50% of EVRAZ activities and operations are based in the Russian Federation, Olga Pokrovskaya's technical and regional experience and qualifications, as a past senior audit manager at Arthur Anderson [*sic*] and as Head of Corporate Finance at Sibneft, is of particular value to the Committee and her experience would be extremely difficult to replicate, particularly as EVRAZ is seeking to strengthen diversity on its Board. The Company considers that, in light of her involvement with the Group over a number of years and her experience in this area, her membership of the Audit Committee is to the benefit of the Group. Furthermore, on 28 February 2012 Sir Michael Peat, an independent non-executive director, was appointed to the Audit Committee, and the Company has therefore been compliant with provision C.3.1 of the UK Corporate Governance Code since that date.

Example 11(ii): Inconsistency in explanation

As of 31 December 2013 EVRAZ complied with all the principles and provisions of the UK Corporate Governance Code (2012 version) with the following exception:
Contrary to provision C.3.1 of the UK Corporate Governance Code, Olga Pokrovskaya is a member of the Audit Committee, but does not meet the independence criteria set out in the UK Corporate Governance Code. More than 50% of EVRAZ activities and operations are based in the Russian Federation, and Olga Pokrovskaya's technical and regional experience and qualification, as a past senior audit manager at Arthur Andersen and as Head of Corporate Finance at Russian oil company Sibneft is of particular value to the Committee. Her experience would be extremely difficult to replicate, particularly as EVRAZ is seeking to strengthen diversity on its Board. The Company considers that, in light of her involvement with the Group over a number of years and her experience in this area, her membership of the Audit Committee is to the benefit of the Group. The Audit Committee includes three non-executive directors, all independent, which we believe mitigates any potential risks.

Finally, in Example 12, the effort to persuade raises three issues: first, an aspect of corporate governance is not thought to be of value (minimization of negative feelings, rhetorical strategy 3); second, the contradictory promise of this issue being fixed; and third, the construction of the second sentence involving a double negative makes the 'explanation' quite clumsy.

The inconsistency and the awkward sentence construction which led the authors to code this to ‘weasel words’ (rhetorical strategy 9b). Why promise to fix something (rhetorical strategy 1c) that the company believes is not a problem and will use up valuable directors’ time and resources? Yet the authors of the Code believe it clearly makes sense for the Chairman to see the non-executive directors without the executive directors being present (for instance if an executive director was to be performance managed) and this remains a relatively uncontroversial item of the Code with which nearly all companies comply (see [Shrives & Brennan, 2015](#)). This explanation *arguably* is not quite as convincing as it should be. Concluding this section, where rhetorical strategies are used together it has to be acknowledged that even though this can be powerful in terms of crafting an explanation, where the strategies are inconsistent readers have to be alerted that the overall explanation as a whole is arguably less meaningful and may even be meaningless.

Example 12: Corrective action promised (1c), Minimization of negative feelings (3) and ‘weasel words’ (9b).

A.1.3 No formal meetings were held by the chairman with the non-executives, without the executives present. The board decided however at its September 2005 meeting that although not anticipated to be of significant value this could not be seen to be against the best interests of the company and have resolved to hold at least one such meeting during the next financial year.

While the ‘comply-or-explain’ system is widely supported, concern persists on the quality of the explanations. The [FRC \(2012b\)](#) introduced the notion of a “meaningful explanation”, which has three characteristics, including “a convincing rationale” (p. 6). Guidance is not provided, and there is no common understanding, on what constitutes “a convincing rationale”, the elements of a “convincing rationale”, and on how to formulate a “convincing rationale”. To this end, we have provided evidence of the use of rhetoric in non-compliance explanations. It is beyond the scope of our methodology to assess whether the rhetoric is convincing to readers. Some explanations lean more towards sophistry than persuasion. Of our nine rhetorical strategies, all might be interpreted as sophistry, other than corrective action and possibly attribution. Concealment/denial (rhetorical strategy 9) is a compelling example of sophistic – hiding something so that what is presented is plausible. However, because certain information is omitted or concealed it is not a totally transparent story. It could be argued that the inherent contradiction of companies claiming their non-compliance is appropriate, and at the same time promising corrective action, is fallacious reasoning. The promise of corrective action, without explaining why non-compliance occurred in the first place, is also a specious argument. Example 1e is a case in point, where the promise of corrective action was never actioned. Thus, it could be argued that the explanation was deceptive, although it is not possible to say whether it was intentionally so. Thus, the rhetorical strategies we found relate more to incorrect or misleading information (sophistry) than to a convincing explanation (rhetoric).

In Section 2, we discussed the power relations between corporates and their audiences. The [FRC \(2016, p. 4\)](#) relies on investors to exercise their power by acting as monitors of the ‘comply-or-explain’ system (“shareholders have every right to challenge companies’ explanations if they are unconvincing”), and for there to be dialogue between company management and shareholders. Given our findings that rhetoric appears to be used more to mislead than convince, we revisit the company-shareholder dynamic. FRC assumptions that institutional investors will exercise their power in monitoring the quality of explanations has not been borne out by prior research, with [Arcot et al. \(2010\)](#) concluding that shareholders have limited monitoring capabilities. [Sergakis \(2013, p. 425\)](#) concludes that investors are “apathetic” even when companies provide insufficient explanation for non-compliance, adding that low shareholder engagement perpetuates poor quality explanations. Given the weak monitoring by shareholders of the ‘comply-or-explain’ system, [Sergakis \(2013, p. 431\)](#) recommends a review panel be established with “monitoring powers” over the quality of non-compliance explanations.

6. Concluding comments

In this paper, we developed a typology to identify the use of different rhetorical strategies in the corporate governance non-compliance explanations. The typology provides a way of not just classifying the strategies used in explanations but also thinking critically about them and whether they are valid. This is important because if companies manipulate their explanations they are undermining the validity of the ‘comply-or-explain’ system. Companies may have incentives to make their non-compliance mimic compliance and readers need to be aware this is happening and to be willing to question those explanations (for instance at the AGM). It may be that we have not yet fully embraced the ‘explain’ nature of ‘comply-or-explain’.

We found extensive use of rhetoric, with minimization of negative feelings (rhetorical strategy 3), the use of ‘weasel words’ (rhetorical strategy 9b) and transcendence (‘ends justify the means’) (rhetorical strategy 4) most common. A trend of increasing use of rhetoric is evident from the comparison of 2004/05 and 2011/12. We also provide some evidence that rhetorical strategies are used in combination. We find some evidence of explanations that do not appear to be substantive and may even be purely symbolic or ceremonial. The FRC indicates that shareholders should raise questions if they are unhappy with explanations ([FRC, 2012a, p. 3](#)), but there is a tendency for (even) institutional investors not to ask questions if performance is not in question. There is a consensus that non-compliance explanations need to be better, but what is better?

By 'lifting the lid' on the rhetorical strategies adopted, we assist investors and others in understanding the crafting of non-compliance explanations. Although some may feel that increased compliance is good, as more companies *appear* to comply, the danger is that the concern for explanations may lessen and investors and regulators may be less likely to interrogate poorly crafted explanations. Compliance can also be seen as a cause for concern. Companies may be tempted to take short cuts in order to demonstrate 'so called' compliance. In many annual reports, it can become difficult to see which items are explanations for non-compliance and which are disclosures trying to justify turning non-compliance into what appears to be compliance. Inevitably, there are inconsistencies between companies. In many ways, the 'explain' part of 'comply-or-explain' is at least as important as compliance. This is because an explanation encourages companies to tell their story of how they are dealing with complex governance issues and is consistent with the spirit embodied in codes since the formation of the Cadbury Committee. In contrast, compliance is silent, can be difficult to substantiate and may not always be authentic.

Non-compliance should, in fact, be welcomed where company directors have made a clear and conscious decision that, in their company's particular circumstance, not to comply is the best approach. Non-compliance should only be questioned where the explanation is poorly crafted, seems inconsistent with other disclosures or does not reflect specific circumstances. Our analysis of non-compliance explanations using a rhetorical lens considering the persuasiveness of those explanations, reveals insights into how non-compliance explanations are crafted, something investors and readers of annual reports might find helpful in their assessment of those disclosures.

This paper has a number of limitations. The typology is not necessarily comprehensive and inevitably involves a degree of judgement. Nevertheless, some important areas have been highlighted and these remain topics for further research. A related rhetorical lens is that of compliance rhetoric. There is some evidence of compliance rhetoric in the explanations, possibly used merely to manage appearances (Parker, 2000). In addition, there is the question of rhetoric versus reality – how does the practical reality within organizations reflect the substance in practice? In this paper, we use of the term rhetoric benignly to mean persuasion. A darker alternative conceptualisation is that rhetoric is used for manipulative purposes (Takala, 1998). Further work needs to examine companies that persistently do not comply for a number of years (serial non-compliers), whether their explanations change over time and any implications this might have on future changes to the Code. Future research could examine the use of rhetoric by non-compliance breach and within industry sectors.

Meaning-oriented content analysis was adopted in this research. While meaning-oriented coding approaches are well established in the financial reporting literature, we acknowledge the limitations of efforts to code segments of text that attempt to establish and standardize their meaning, which may frustrate retrieval of the nuanced meanings that explain action (Biernacki, 2014). In relation to interview data, Augustine (2014) suggests an alternative analytical approach that does not entail coding – rather she uses writing and reading (about and of the interview data) as methods of inquiry and analysis. Biernacki (2014) advocates a humanist approach where context is integral to the determination of meaning. Explanations for non-compliance should be customized to context: should "set the context and historical background" (FRC, 2012b, p. 6). Discourse analysis may offer an alternative methodological approach for future research, taking into consideration the wider context.

Do readers care about 'comply-or-explain' disclosures? Further work relating to the impact of rhetorical strategies on readers is also needed (see Stanton, Stanton, & Pires, 2004). In particular, are certain rhetorical strategies (alone or in combination) more effective than others at convincing readers? We believe that where rhetorical strategies are used together they are likely to be more convincing but they may not be better explanations. Finally, continued efforts are required to convince company managers and regulators of the importance of a properly working and authentic 'comply-or-explain' system of corporate governance. To this end, we believe that as much emphasis should be placed on 'explain' as 'comply'.

Rhetoric is influenced by culture. Rhetorical strategies in the UK may not be the same as in other countries. Indeed, rhetoric may be different across organizations and sectors. Future research might factor the effect of culture on the rhetoric in corporate governance non-compliance explanations, possibly across jurisdictions with 'comply-or-explain' systems.

The FRC's (2012b, p. 6) characterises the 'comply-or-explain' system as "widely admired and imitated internationally". However, some respondents on the 'comply-or-explain' system do not share the same view, describing explanations as "of limited use", "not . . . adequate", "boilerplate", "lack of credibility" (FRC, 2009, p. 37–38). In the FRC's (2012c, p. 44) celebration of the 'comply-or-explain' system, chairman of Anglo American plc, Sir John Parker, dismisses these criticisms by stating that ". . . this is a failure of the application of 'comply-or-explain', not the principle itself". Our evidence contributes to the debate on the application of the 'comply-or-explain' system, specifically what kinds of explanations are appropriate. Findings from our research indicate that more guidance is required from regulators on what constitutes a 'convincing rationale'.

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