

Global Roundtable Series

Corporate Governance for a Changing World

Compilation of Executive Summaries:

New York, London, Zurich, Breukelen, Brussels, Paris, and Oslo



The Purpose of the Corporation Project, an initiative of Frank Bold with the support of the Modern Corporation Project at Cass Business School, launched the Global Roundtable Series: Corporate Governance for a Changing World. Events were held at major business centres around the world, including London (Cass Business School, Sept 2014 and 2015), New York (NYU Stern School of Business, June 2015), Zurich (University of Zurich, October 2015), Breukelen (Nyenrode Business School, February 2016), Brussels (EurActiv headquarter, Brussels 2016), Paris (Fondation Charles Léopold Mayer, April 2016), Oslo (University of Oslo, August 2016). All events took place under the Chatham House Rule.

The series brought together more than 260 leaders in business management, investment, regulation and academic and civil society communities with the aim of identifying desired outcomes and principles of corporate governance fit for the challenges of the 21st century. In these roundtable events, we explored the deliverables that corporate governance should contribute to long-term sustainable value, as well as the pathways to achieve them, in order to clarify appropriate structures and practice. This document draws together all the executive summaries produced after each roundtable.

The highlights from this roundtable summary have been included in ‘Corporate Governance for a Changing World: Report of a Global Roundtable Series’ available at http://www.purposeofcorporation.org/corporate-governance-for-a-changing-world_report.pdf. The report was launched at a high-level policy oriented conference in Brussels on September 28, 2016, and presents an emerging comprehensive approach to corporate governance that can assist corporations to focus on a broad understanding of their purpose, long-term sustainable value, building resilience, and sustaining a strong social license.

About

Frank Bold is a purpose driven law firm using the power of business and non-profit approaches to solve social and environmental problems. With six branches in three EU countries, Frank Bold provides legal expertise in corporate accountability to the European institutions as well as to NGO’s in many countries. Together with the Modern Corporation Project, Frank Bold initiated a collaborative project on the [Purpose of the Corporation](#) which brings together business, regulators, civil society and academics to forge a new vision for the future of corporate governance and company law, and more generally the role of business in society.

The academic basis for the project is provided by Dr. Jeroen Veldman and Prof. Hugh Willmott, who run the Modern Corporation Project at Cass Business School, London (themoderncorporation.org).

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Co-hosted by: Aspen Institute Business and Society Program, Cass Business School, the Conference Board Governance Center, Frank Bold and NYU Stern and Law

How should corporate governance contribute to robust long-term value creation for companies? What corporate governance practices can help companies manage and develop intangible assets more effectively? Amidst incredible complexity and increasing societal expectations on corporations, what should society realistically expect from corporate governance with respect to environmental and social issues?

These were the main questions discussed at New York University School of Law on June 11, 2015 by 25 leading corporate governance experts. The roundtable brought together a unique mix of business and law professors, institutional investors, company representatives, and civil society organisations. The event was the second in a global corporate governance roundtable series launched by the Purpose of the Corporation Project. It was co-hosted by NYU Stern and Law, Aspen Institute Business and Society Program, the Conference Board Governance Center, and purpose-driven law firm Frank Bold that initiated the aforementioned project in Europe.

Unpacking the elements of long-term sustainable value

Filip Gregor, Head of the Responsible Companies Section at Frank Bold, launched the afternoon by noting that the Anglo-American corporate governance model has shaped governance in continental Europe due to the influence of the OECD through its Principles for Corporate Governance and the EU. Now that the financial crisis has revealed weaknesses in this corporate governance model, it is appropriate to have a trans-continental debate about the way forward. He suggested that underlying corporate governance regulation is the tension between short-term and long-term investment: “only short-term is bad, only long-term is bad; it’s about striking a balance between the two”.

Intangible assets and economic value

David Langstaff, CEO of Argotyche Inc., asked roundtable participants in the first session to consider how companies should (1) account for, (2) measure and (3) deliver intangible assets.

Several participants noted that there now exist many metrics for short-term but not long-term value. Current accounting models are limited in terms of what they measure and their time horizons. Environmental, social and governance (ESG) matters have an impact on performance but are mostly qualitative and therefore difficult to measure. It is similarly difficult to measure complex concepts and intangible assets such as resilience, leading most indicators to typically rely on proxies.

There is a constant trade-off between simple and easy to use quantitative indicators and relevant, high quality qualitative indicators. For example, ISS’s quantitative model is easily comparable and useful for busy asset managers but lacks a nuanced analysis and may ultimately direct our focus towards what is readily counted rather than what counts. Yet the reality of high-frequency trading must be acknowledged, which increases the pressure on boards and firm leaders to focus on financial indicators.

One discussant pointed out that the debate how to measure non-financial assets dates back several decades. The balanced scorecard approach developed by Kaplan was widely used in the 1980s and 1990s and could

be a useful model for combining financial and non-financial metrics (see Kaplan and Norton, 2001). Other non-financial metrics are being developed by organisations like the Drucker Institute and the Sustainability Accountability Standards Board (SASB).

On the other hand, a participant asked whether the ultimate goal is to put a financial value on intangible assets at the company level, and whether it should be? A number of participants noted the importance of telling a compelling story about the company's long-term strategy. Many investors appreciate having direct conversations with the leadership team about where the company is headed; this may be more informative than relying on imperfect metrics.

It was asked what must change and where to start with this transition: how should we reward a company for good governance? One participant suggested that it may be necessary to change stock exchange rules or other regulations in order to give companies the space to reap the reward of long-term investments and doing the 'right thing'. Another suggested changing the tax code to create incentives for holding shares long-term, e.g. by reducing capital gains tax payable on shares held long-term, as has been urged by BlackRock's CEO (see Sorkin, 2015). Investors may also play a role here; one investor in the room had put forward a shareholder resolution to split the CEO and Board Chair positions in order to push the relevant company to overhaul its governance structure and take responsibility for a human rights disaster in which the company had been implicated. Similarly, investors (and regulators) ask for detailed information about top executive compensation without requesting any details about the salaries of workers at the bottom.

The question was posed whether the problem of how to promote responsible business is a structural issue or a behavioural one. Participants agreed that tone from the top is important as it creates brand and trust, CEOs that recognise the value and importance of sustainability need to communicate proactively with employees and shareholders to embed this way of thinking into the corporate image. One participant suggested that the root challenge is that the shareholder primacy model of corporate governance perceives expenditures on intangibles such as human capital to be a waste of shareholder assets and consequently not made a priority by many business leaders.

Environmental and social value

In the second session, Karen Brenner, Executive Director of Law and Business Initiatives at NYU asked the room to consider what society should realistically expect from corporate governance with respect to environmental and social issues.

Michael Posner, Professor of Business and Society at NYU then provided context for the discussion, noting that corporate social responsibility (CSR) is not central to business strategy and identifying the need for industry-specific identification of human rights risks. For example, the food and beverage industry is plagued by issues relating to agricultural sustainability and working conditions, especially of migrant workers, and these issues should be reflected in any human rights standard used to judge that industry's performance. Prof. Posner suggested that benchmarks should look at outcomes in addition to process and commitments. In other words, "trust, but verify", as we are past the point when all companies can be on a journey to human rights and they should therefore be judged on their outputs.

There may also be a place for voluntary industry initiatives. For example, the Private Military Code gives guidance on the use of force while Oxfam's Behind the Brands scores the ten largest food brands on a range of food justice issues, including water, land and climate change. Ideally investors should be pushing firms to engage constructively with human rights issues. Consumers will also drive the shift to real sustainability by picking competitors who rate well on various indicia. The Shift Project has developed a corporate human rights benchmark designed to measure performance against the core human rights instruments (known as RAFI).

Governments are beginning to demand more information from their own companies, although they continue to lag at adequately respecting and enforcing human rights standards. The primary emphasis is on disclosure of risk, e.g. the US Dodd Frank Act requirement to disclose information on conflict minerals, the UK's Modern Slavery Act, and the EU Non-Financial Reporting Directive. Each of these legislative instruments contains detailed disclosure requirements but has limited provision for monitoring or enforcement.

Exploring solutions

Future Scenarios

Participants engaged in a backcasting exercise led by Rick Wartzman, Executive Director of the Drucker Institute where they were asked to design a corporate governance innovation to address a challenge facing a mock company (see e.g. Quist and Vergragt, 2006 for an explanation of backcasting). Each group was asked to assume a different position (CEO, board of trustees/directors, institutional investor) and then tackle a different environmental or social challenge to prompt reflections on how to stimulate positive changes through corporate governance in the next five years.

The group playing the role of institutional investor on the board of a public company explored various options for increasing their influence, including creating an investor role on the board (along with a directorship for stakeholders), an investor advisory committee to the board (similar to technology, Silicon Valley advisory committees) or shifting to a principles-based disclosure regime in place of the current rules-based one. The group eventually decided instead to stagger the board and extend the length of term for each director from annual elections to three to five year terms with a reasonable recall trigger. The thinking was that annual elections add some accountability but they create a 'campaign mentality' that prevents directors from focusing on long-term value creation.

Another group wished to encourage long-term investors by creating different classes of dividends. They decided to create time-weighted dividends with increasing payments made to investors that remained for the long-term, as compared to current dividends that pay out a flat per share amount to all shareholders regardless of the length of time of their shareholding. Introducing time-weighted dividends would be easiest for private companies at the moment of listing as their decision would be protected by the business judgment rule as well as state law, federal law and stock exchange listing rules (see Belinfanti, 2014: 850- 52). For public companies, it would likely be necessary for these firms to first go private before relisting, or amend existing listing rules, before this innovation could be adopted.

The group representing senior management explored the implementation of a compensation system for managers that would emphasise intangible assets and ESG matters. A key element of this innovation was the connection with long-term risks and opportunities. A well-functioning compensation system should go hand-in-hand with a defined long-term business strategy and the integration of sustainability. In this respect, it would incentivise as well as depend on a functional collaboration between the board of directors and senior executives.

The group representing regulators focused on a flexible but mandatory system for the disclosure of ESG matters by public corporations. Such a system would be designed in a way to create a safer space for exploring disclosure by corporations and would aim to facilitate the debate between corporations and long-term investors, in particular institutional ones. Similarly to the discussion in the previous group, the discussants emphasized the connection of ESG disclosure to long-term corporate strategy.

Additional innovations that were explored:

- Loyalty shares, which could encourage long-term investing by giving shareholders a reward after a pre-

determined time period, such as by giving investors the right to buy additional shares at an advantageous price or granting special bonuses (see Peterson, 2011).

- Dual-class share structures, which have been widely used by the founders of US technology firms such as Google and Facebook to retain decision-making authority while bringing on board capital from external investors.

How can we get there?

Lynn Stout, Distinguished Professor of Corporate and Business Law at Cornell Law School, asked the room what can be done by the experts in the room to create momentum for potential reform. Prof. Stout inquired whether there might be a role for non-traditional corporate governance actors, such as labour, consumers, academics, socially responsible investors (SRIs) and proxy advisors.

It was suggested that the framing of the future of corporate governance should deliver a positive message, i.e. that good business behaviour is a win-win that will translate into strong financial performance over the long-term (see e.g. Mitchell et al. 2015). The goal should be to create a 'race-to-the-top', not necessarily to criticize poor performers or resort to an adversarial position vis-à-vis companies that lag behind. Another participant, however, suggested that the use of 'sticks' in addition to 'carrots' should not be underestimated and that there may be value in trying to measure and evaluate the companies that do not perform well. More work is needed to foster an environment where companies feel free to step up to the table to address their impact. We should be positioning sustainability as an opportunity for companies to reduce risk in the face of looming crises, such as climate change, that will have a detrimental impact on businesses that fail to adapt. Institutional investors could be a key avenue to bring CEOs to discussions of how to address these issues.

Several concrete proposals for next steps emerged, including:

- Mapping institutions and organisations that are already taking on the challenge of addressing short-termism in order to identify key players.
- Mobilising allies quickly to respond to current events with op-eds and media interviews explaining how the events relate to underlying structural issues, e.g. how an eventual future financial crisis is tied to the failure to overhaul the regulatory system. This could be done through a listserv or a loose network of scholars, such as been assembled by Dr. Jeroen Veldman of Cass Business School.
- Strengthening connections between socially responsible investors and civil society organisations as a coordinated effort.
- Convening institutional investors at the CEO level to align interests and as a group create pressure for long-termism.

Final thoughts

Donna Dabney, Executive Director of the Conference Board Governance Center, wrapped up the session by noting that the quest to create metrics for intangible assets goes back decades to the balanced score card of yesteryear. Institutional investors have said 'enough metrics, tell us your story'.

Multiple participants suggested that sustainability will become imperative for growth in the near future, not a value-add or a risk management issue. Currently, however, there continues to be a disconnect between the rhetoric in support of investing in sustainability and long-term value creation, and actual investment practice. Large institutional investors have begun to establish dedicated ESG units but these arguably remain marginal to their conventional investment activities, which continue to focus first and foremost on traditional financial indicators. It was suggested that regulatory intervention might be necessary to address this inconsistency.

As one participant noted, “we are trying to jumpstart a cultural change”, which requires a multi-prong approach of both voluntary and regulatory initiatives.

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Cass Business School
CITY UNIVERSITY LONDON

Co-hosted by: Cass Business School, Frank Bold and Tomorrow's Company

Environmental and social sustainability issues are material financial matters posing both opportunities and risks to the long-term success of companies and the economy as a whole. In recent years, consensus has begun to emerge that firms should focus on creating long-term sustainable value. Leaders in the business, investor and other communities now realise that we must integrate sustainability into the core of our economic system. Amidst complexity and increasing societal expectations on corporations, it remains unclear what corporate governance should deliver in terms of addressing environmental and social issues.

At this event we were joined by Dr. Roger Barker of the Institute of Directors (UK) for a deep-dive session on corporate governance designed for company secretaries, senior management and board directors. The facilitated roundtable discussion gave participants the latest information on best governance practices and regulatory developments, and discussed how to ensure effective governance delivery to internal and external stakeholders.

How can corporate governance address the conflict between market demand for strong short-term performance and the longer perspective necessary for sustainability?

Keynote speech by Roger Barker of the UK Institute of Directors

Roger Barker opened the discussion by arguing that the UK corporate governance model fails to foster a long term business approach because listed companies place a much greater value on immediate returns at the expense of investing in long-term economic viability. This dampens innovation and limits research and development, hiring, and the ability of companies to be environmentally sustainable, all of which negatively affects UK's competitiveness.

What can we do to counter these short term tendencies? First we must acknowledge the problem, which is disputed particularly by fund managers in the City of London. Many believe the UK has an excellent governance system that protects minority shareholders, subjects managers to market discipline and allows activists and take-over threats to discipline wayward managers.

.....
"Short termism is one of the fundamental fault lines of our economic model."

Roger Barker

The Kay and Cox Reviews concluded that these beliefs were misfounded. Academic research at the Bank of England, especially by Mervyn King (1973) revealed the market discount rate for the valuation of investment streams and opportunities.

John Asker, Professor of Economics at UCLA (2014) reviewed financial studies comparing the behaviour of stock market listed and privately held companies across a large data-set of US enterprises, comparing similar firms in terms of size, sector and other variations. The research concluded that privately held companies systematically invested in the long-term more than listed companies, and listed companies that were least responsible to potential investment opportunities were in sectors with the highest share price volatility.

It is no surprise that public shareholders are more short-term since liquidity is more easily achieved for public shares than private ones, so a longer-term view is normally taken by those held privately. The average holding period for British and American equities has declined from over six years in 1950 to less than six months today. More than half the daily turnover is undertaken by short-term trading by high frequency traders and hedge funds. Mr. Barker questioned the conventional wisdom that six months is an average with pension funds and insurers holding long-term liabilities taking a longer perspective. Institutional investors held approximately half of equities in the 1960s but now represent only about 15% of UK equities. Furthermore, since the 1990s the process is now outsourced to fund managers that are mandated to a beta-benchmark over a specified time scale. Spence Johnson (2014) found that UK pension funds give their fund managers approximately 12 months to recover from poor performance, down from 20 months in 2008.

Taken as a whole, this suggests that investors are increasingly short-term oriented. The pressure is transmitted to company behaviour through executive pay over relatively short time horizons (typically three years), which encourages share buybacks at the expense of long-term investments (Smithers 2012).

Mr. Barker argued that a deeper issue is that professional advancement is tied to advocating faster rates of change and return. For example, Barclays CEO Anthony Jenkins seems to have been ousted due to an internal impatience that led to the board of directors losing faith with him after only a few years, without any clear external demands for his replacement. This impatience has contributed to a median CEO tenure that has decreased to less than five years.

It is naturally more challenging to identify the solution than the problem. Mr. Barker suggested that shareholder primacy continues to be a workable model of corporate governance, as was concluded by the company board steering group before the adoption of Companies Act, 2006. He disagreed with recent arguments by the Bank of England (Haldane 2015) and Financial Times economist Martin Wolf (2014) that England should move to integrate stakeholder voice into governance, such as by giving employees a seat on the board. Mr. Barker posited that shareholder value creation need not be equated with maximising short-term profits or share price (described by former GE CEO Jack Welch as the ‘dumbest idea in the world’). Investor short-termism, in Barker’s opinion, arises from the lack of a major controlling shareholder in the modern UK shareholding structure, which could shield companies from share price fluctuations, hostile takeovers and possibly foster a longer term outlook.

While many argue that European companies perform well with a pluralist stakeholder approach, Mr. Barker suggested that it was rather their more concentrated ownership structure, often based on strong family ownership in listed companies, which enabled them to take a longer-term perspective than their UK counterparts.

Multiple voting structures: a plausible option to foster long-term investing?

Perhaps the best option for the UK context would be to find a way to give longer term shareholders more control over listed companies or incentivise investors to take a longer term approach. One mechanism to achieve this is the more widespread adoption of multiple voting/loyalty shares, which are prevalent in countries such as Sweden, France and Denmark. In France, the loi Florange (2014) set the default so that shareholders will double their voting rights after two years. Companies may opt out of this default through a shareholder vote. In the US, it is common for companies to list with dual class (A and B) share structures whereby the B shares may lose their voting

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“What we need to realise is that all companies are different and therefore need a differentiated approach to governance. Corporate governance is not one-size-fits-all. I fear that the current system in the UK is too focused on protecting minority shareholders and exerting short-term financial discipline.”

Roger Barker

privileges if traded to another party. The objective is to concentrate power in the hands of shareholders that are interested in long-term control. Dual class share structures are particularly common within Silicon Valley technology firms where they represent 7% of all companies, including Google, Facebook and Amazon, as well as media conglomerates such as the New York Times (Fenwick and West 2014).

Institutional investors often oppose differentiated voting rights as they perceive them as a means for larger blockholders to strengthen their control at the expense of minority holders. Earlier this year, UK investors successfully campaigned against a new law in Italy that would have doubled voting rights for long-term shareholders, arguing that it would deter foreign investment.

Mr. Barker suggested that multiple voting structures should be permitted on the London Stock Exchange to allow UK-listed companies to compete with their rivals in the US and Asian technology industries, provided the process is transparent and appropriate to the company. Multiple voting structures would prioritise patient and informed shareholders that understand the company's strategy and are prepared to take the longer term view in the face of significant uncertainty under potentially difficult financial circumstances.

Recent global regulatory changes and developments

Presented by Paige Morrow, Head of Brussels Operations at Frank Bold

The G20/OECD Principles of Corporate Governance were released on September 5, 2015 with revisions that focus on protecting minority shareholders, increasing financial disclosure and promoting say-on-pay. While non-binding and non-prescriptive, the Principles are highly influential on global corporate governance trends. The OECD has launched a Trust and Business Project to promote a discussion about the effective integration of business integrity considerations into a company's decision making. This underpins the responsibilities of the board and executive management (as defined in the Principles) and aims to help companies better mitigate the risk of serious corporate misconduct.

At the EU level there have been several relevant developments affecting corporate governance and company law, including the revision of the Shareholder Rights Directive. The revision passed a plenary vote in European Parliament in July 2015 and is proceeding into trilogue negotiations between the Council, Commission and Parliament in autumn 2015. The Parliament eventually rejected proposals from the Legal Affairs Committee that would have introduced incentives for long-term shareholding and allowed workers to give an advisory opinion on senior executive compensation schemes. Highlights of the revision include:

- a recognition in EU law that shareholders do not own publicly traded companies,
- the introduction of tax transparency requirements that would introduce country-by-country reporting (that exceed the minimum requirements suggested by the OECD), and
- a non-binding say-on-pay and the requirement that institutional investors and asset managers adopt an engagement policy that monitors environmental and social risk.

An important development coming up on the horizon is the Directive on disclosure of non-financial and diversity information, which will require more than 6,000 large EU businesses to report on environmental matters, social and employee-related aspects, respect for human rights, anti-corruption and bribery issues, and diversity on boards of directors as of 2017. The underlying aim is to improve corporate governance by increasing transparency and pushing companies to prioritise the disclosure of extra-financial information.

As part of its package on corporate governance and company law, the EU is also contemplating the adoption of a common framework for single-member limited liability companies (commonly referred to as 'Societas Unitas Personae' or 'SUP'). The objective is to facilitate cross-border business activity for micro-enterprises and SMEs.

Key characteristics of SUPs would be the availability of online registration, only 1 euro/pound minimum capital reserve, lack of stipulation for employee representation, and labour law being covered by existing national laws.

Concerns have been raised by observers about the lack of size restrictions on SUPs, which would their facilitate their use by large companies, to evade tax rules or for money laundering; the lack of protection for both creditors and employees; and the possibility of splitting the company's registered seat and the place of central administration (which has implications for issues relating to employment, tax and eventual bankruptcy proceedings).

Future Scenarios

Moderated by Filip Gregor, Head of the Responsible Companies Section at Frank Bold

Breaking into small groups, participants debated what corporate governance innovation could be adopted by listed companies to address short-termism. Each group assumed a different role (CEO, board of trustees, institutional investor) and then design a corporate governance innovation to foster long-termism. Looking 25 years into the future, each group was asked to visualised the successful implementation of their idea and work backwards to identify the major milestones along the way to success, the barriers that were overcome, and the allies that supported implementation (see e.g. Quist and Vergragt, 2006 for a more detailed explanation of backcasting)

Quadruple Bottom Line - Purpose

The first group, representing the board of directors, added a fourth 'P' to the concept of the triple bottom line (people, planet and profit) to include 'purpose' or 'principle'. The company intended to articulate its long-term purpose, either an objective that was immediately achievable or could be achieved within 10 years. It was agreed that support was needed from both internal leadership - in particular from the board - and shareholders. Motivation is crucial to integrating sustainability into the business.

The group examined two interesting case studies: reference was made to the introduction of hotel reuse towel programmes. The use of cards asking hotel guests to reuse their linens, which has become standard practice in millions of hotel bedrooms worldwide, began with the vision of a board member at International Hotels Group. The group also discussed the challenge of articulating an ethical purpose for the global jewellery industry in order to 'do the right thing' for primary producers and ensure that conflict diamonds do not enter the market.

Articulation of successful, sustainable business vision

Another group represented the management team and started their discussion with the interconnected questions of what the world is going to be like in 10 years' time, and what is needed to succeed in that world? They agreed that many of the challenges businesses are already grappling with - including resource constraints, the potential impact of climate change and population increases and water shortages - will become increasingly predominant. The group decided to articulate a vision for how a successful business needs to operate now and into the next 10 years to continue to be successful and make a positive contribution to addressing the identified global challenges.

The first aspect in implementing this vision was to articulate a business strategy that took sustainability seriously and internalised impacts that are presently considered externalities, e.g. noise pollution, carbon emissions and over harvesting of fish.

The second strategy was to use education within the business at every stage of employment: recruitment, training and ongoing education, and also to challenge business school to teach differently by funding courses, curricular development and professorships designed to instill a different way of thinking and operating in business.

The third step was to redesign the company's incentive structure for every level of employee to ensure that middle managers and frontline employees were aligned with the same incentives as those of senior leadership.

The fourth element was to communicate to investors that the company would be focused on the long-term (similar to what Paul Polman did when he became CEO). The company would then report on how it was delivering on its purpose by integrating his into its reporting framework, such as that developed by the International Integrated Reporting Council (IIRC), which requires reporting on the six capitals (environment, manufactured, intellectual, social, financial and human).

The group suggested that the CFO should take ownership of reporting on sustainability and a board member would be responsible for oversight to ensure that it became part of the organisation's decision-making structure, rather than be consigned to an isolated CSR/sustainability department. It was considered important for the process to be done transparently with a public commitment to change in order to allow customers, investors and employees to judge implementation against clear benchmarks.

Complete integration of ESG into business strategy

A group representing institutional investors decided to integrate ESG factors into mainstream fund management and eliminate the consideration of these elements by a separate ESG analyst or department. It was considered that this would be a way to embed this way of thinking into the way that all fund managers make investment decisions and reinforce the point that ESG factors drive investment performance for all classes of assets.

It was recognised that the accumulated evidence of the link between ESG and financial performance needed to be better communicated to fund managers. A significant challenge is the preference for quantifiable indicators, which creates a challenge for measuring qualitative aspects of performance, such as the ability of a business to innovate and develop valuable new products.

At the same time, end beneficiaries should be expressing their desire to see ESG issues integrated into investment decisions to the trustees or fund managers. Additional factors include financial regulation and voluntary codes, such as the UN-supported Principles for Responsible Investment (UNPRI). The general trend is to push funds towards greater transparency of how they incorporate ESG issues into investment decisions and report on the ESG-performance of companies. On a somewhat dispiriting note, the group acknowledged that an external disaster would likely help to shake companies and fund managers into taking sustainability issues seriously and respond to the risk of climate change.

Reporting on corporate purpose

The last group was composed of regulators, who were split on the action that should be taken to push boards to consider the long-term consequences of their actions. They agreed that companies should be required to report on the purpose of the company and this could include an explanation of how the company is delivering on the public good or around a business model such as 'B Corps'. Some participants favoured the use of incentives such as tax benefits, while others were skeptical about the unintended consequences of manipulating tax rates without first studying the expected impact. There seemed to be consensus that companies should be encouraged to behave more like citizens in terms of their impact on the world. The question left to answer was whether companies should be rewarded for good behaviour, and if so, how.

Identifying the main corporate governance challenges and opportunities over the next decade

Moderated by Stefan Stern, management writer and visiting professor at Cass Business School

In the concluding session, participants discussed the extent to which corporate governance regulation should be revisioned. As a preliminary question, a participant asked the other experts in the room whether they thought that boards should be primarily focused on steering or supervision. While there was consensus that boards should fill both roles, the difficulty was in gauging the right level of attention to devote to each responsibility.

Governance may have become excessively compliance-driven such that it creates a risk averse culture that stifles value creation, risk-taking, creativity and innovation. Yet markets and regulators may react negatively to boards that deprioritise risk management and boards expose themselves to potential liability for failure to properly fulfill their duties.

Several participants said that we need inspired leadership that creates positive internal culture and understands what drives behaviour at all levels within a company. A number agreed that the current approach fails to look at the drivers that lead individuals to make decisions that cause negative externalities, such as water pollution or the emission of toxic chemicals that contribute to global warming.

One participant thought that positive incentives should not be introduced to foster pro-social behaviour, but rather incentives that promote short-termism should be removed in order to allow individuals to make decisions that will benefit businesses and eventually reduce the need for external regulations. People often want to 'do the right thing' but may be constrained by external factors, peer pressure or simply responding to signals from others ('group think').

Given the need to improve sustainability literacy, core business school education should be reformed to ensure future business leaders have the tools they need to examine how their companies create value and the impacts of their business have on both internal and external stakeholders.

Others disputed the continual emphasis on solutions coming from companies themselves and suggested that regulation needs to be combined with internal solutions. Businesses themselves may benefit from regulations that set clear expectations for behaviour.

There was significant difference of opinion on whether the Corporate Governance Code gave businesses the right level of flexibility to tailor solutions to fit their needs or rather had become dysfunctional. One controversial proposal was to drop the UK Corporate Governance Code in favour of increased reliance on the seven duties of directors, which are set out in the Companies Act. While others disagreed with scrapping the Code, there was recognition that regulation has multiplied and in many instances become overly process-oriented.

Finally, it was suggested that the fundamental problem with regulation is that it continuously multiplies and becomes increasingly complex to address past events and crises. The current focus on risk management is understandable as it is in reaction to the global financial crisis. Societal expectations of companies have evolved and it may be appropriate to broaden the duties of directors to more explicitly address business impacts.

Directors' duties as set out in the Companies Act:

- Duty to act within powers (s. 171)
- Duty to promote the success of the company (s. 172)
- Duty to exercise independent judgment (s. 173)
- Duty to exercise reasonable care, skill and diligence (s. 174)
- Duty to avoid conflicts of interest (s. 175)
- Duty not to accept benefits from third parties (s. 176)
- Duty to declare interest in proposed transaction or arrangement (s. 177)

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Cass Business School
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The logo for Frank Bold, consisting of a red stylized 'F' icon above the text 'Frank Bold' in a bold, red, sans-serif font.

**tomorrow's
company**

Co-hosted by: Cass Business School, Frank Bold, the Institute for Business Ethics at University of St. Gallen and the University of Zurich Centre for Human Rights Studies

Frank Bold in partnership with the University of Zurich Centre for Human Rights Studies and the Institute for Business Ethics at University of St. Gallen held a roundtable on the purpose of the corporation and the future of corporate governance in Zurich on October 29, 2015. The roundtable was a part of the series organised by the Purpose of the Corporation Project with support from the Modern Corporation Project based at the City University London Cass Business School.¹ Keynote speeches were given by Christopher Wasserman, CEO of Terolab Surface Group, and Katrin Muff, dean of Business School Lausanne.

Introduction - Filip Gregor, Frank Bold²

Corporations are a man-made construct that require societal approval to exist. Business leaders are accountable not only to shareholders, but shareholder value has become an increasing focus. After the latest financial crisis, which many have argued was rooted in an excessive focus on shareholder value maximisation, the topic of corporate governance has experienced renewed interest. However, policy-makers have proposed solutions focused almost exclusively on encouraging more shareholder engagement.

In the previous events of this series in London and New York, several proposals for concrete changes emerged:

- Specify corporate purpose
- Clarify the fiduciary duties of directors in corporate governance
- Engage other stakeholders in corporate governance
- Review executive compensation rules
- Incentivise long-term shareholding

The aim of the Zurich roundtable and future events is to review the viability of these proposals, develop additional ideas and address several remaining questions:

1. What is long-term sustainable value?
2. How can good quality management be reflected in better results?
3. What is the role of investors?
4. How can we better reflect sustainable value?
5. What is the best framing and language for this discussion?

Christine Kaufmann, Centre for Human Rights Studies, University of Zurich³

American economist Milton Friedman (1970) argued that the role of business was to focus on increasing profits as long as it stayed within the rules of the game. Since then there has been an ongoing debate about the role of business in society. The Swiss Federal Council had difficulty developing a definition of corporate social responsibility when it undertook to write a position paper on CSR.

The current debate in Switzerland on responsible corporate behaviour is divided into three areas of focus:

1. UN Guiding Principles on Business and Human Rights - The Swiss National Action Plan on Business and Human Rights is expected at the end of 2015.
2. OECD Guidelines for Multinational Enterprises - New procedural rules have been developed for the National Contact Point. The Swiss Federal Council also adopted and published a CSR Position Paper in April 2015 which defines the government's expectations of companies in the area of CSR.⁴
3. Business initiatives - Voluntary efforts by business to define CSR include the Swiss Code of Best Practices on Corporate Governance⁵ (led by Economiesuisse), as well as a recent publication named « CSR from a Business Perspective » (led by SwissHoldings and EconomieSuisse)⁶ and company-specific approaches.

There is reputational risk for Switzerland if its companies fail to act in a responsible manner. Corporate responsibility is also in companies' own interests as sustainability is a driver of lasting economic success. At the same time, there is a lack of discussion by policymakers and business leaders about value that is not reflected in balance sheets.

While Switzerland has not until now exercised political leadership on responsible business issues, there are some signs that standards are rising. There are a variety of initiatives that attempt to implement responsible business, including the Swiss Federal Council's position paper on CSR the ongoing development of a Swiss National Action Plan on Business and Human Rights; and pending legislative proposals, including financial transparency obligations for the extractive industry, the revision of the Swiss public procurement law to include sustainability, food speculation and popular initiatives on food speculation and responsible business.

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Swiss Position Paper on Corporate Social Responsibility - 1 April 2015

“The Federal Council expects companies to take responsibility for their impact on society wherever they conduct business, in Switzerland and abroad.”

There is agreement about the need for responsible business but a lack of clarity about the broader picture: what is the purpose of the corporation? What does it need to produce wealth in a sustainable manner? What governance issues exist? Does it need to produce wealth? In Switzerland this broader debate is only beginning. We should address these questions directly before developing more detailed strategy to address the role of corporations in the society.

Christopher Wasserman, Foundation Ecophilos, Zermatt Summit Foundation and TeroLab Surface Group⁷

Mr. Wasserman suggested that in addition to corporate governance, we should recognise that the current economic framework is unsustainable. He asked the room to consider how we should shift from capitalism to post-capitalism, reflecting that the world has changed. As shareholders, we must develop a roadmap towards socially desirable progress. TeroLab Surface, Mr. Wasserman's company, has adopted a number of initiatives to integrate responsibility and sustainability in its business, including the Blueprint for Better Business' model for leadership, ISO 14000 and integrated reporting.

Mr. Wasserman suggested we should think from the outside in:

1. Look at companies' compliance with corporate governance guidelines.
2. Identify and measure important sources of value or loss that do not currently show in the balance sheet, such as human capital or environmental value.
3. Improve employee training and engagement to sharpen their understanding of sustainable value. It may be advantageous to give small groups within the business responsibility for different aspects of sustainability.

Responsible leadership comes from the top but at the same time management is undergoing a revolution as we recognise that top-down management is not working anymore. Millennials, in particular, do not automatically recognise and accede to authority.

New accounting standards are needed as traditional accounting frameworks do not capture human capital or externalities. Integrated reporting is one way of capturing intangible assets and value. Tax incentives would also encourage responsible behaviour. Finally, we need to think about how we can ensure better access to capital for responsible businesses.

Katrin Muff, Business School Lausanne⁸

Prof. Muff highlighted the need to step back and embrace first the bigger and broader picture. She suggested that we consider corporate governance in the context of the challenge of living well on one planet, which is the [WBCSD Vision 2050 goal](#). A participant noted a challenge is to translate corporate governance from reporting to strong management.

Prof. Muff suggested that we frame corporate activity within the “safe operating space” of the doughnut model developed by Kate Raworth and Oxfam⁹. The doughnut model presents a visual framework in the shape of a doughnut that brings together the concept of planetary boundaries and the complementary concept of social boundaries. Although there is increasing recognition of the need to live within the boundaries of our planet’s resources, no regulatory framework uses the doughnut model. Instead the current focus is mainly on voluntary action.

Ms. Muff suggested that regulatory signals are critical to trigger a significant shift in behaviour. The disconnection between the good initiatives that more and more businesses take on sustainability and the challenges facing us – or the lack of progress on the macro level on sustainability - is far greater than in 1992 when global leaders adopted the Rio Declaration on Environment and Development. We need to question this gap: why have business initiatives not led to more global improvement? What new models of company governance need to be developed?

Group discussions

In groups, the participants discussed the disconnection between the macro-level economy and the micro-level of individual corporations. There was general consensus that we need to redefine shareholder value and address the disconnection.

Strengthening voluntary action by companies:

One participant observed that regulatory reactions to crises will always occur ten years too late. It is therefore arguably necessary to strengthen voluntary business action and develop incentives for good behaviour but there was disagreement about whether the correct response was to focus on voluntary or mandatory rules.

Corporate governance as an answer to the problems of business:

It was suggested that corporate governance should be revisited in the context of a holistic assessment of changes to the way that organisations are run. What does a value-based recruitment and incentive system look like? What is the role of values in sustainable organisations? How can we recognise and create value?

A participant argued that the role of corporate governance is not only to protect the company but to ensure that a corporation is able to create value for society at large. In the financial sector, financial market regulations

have been internalised within corporate governance while this is just starting to emerge in the context of climate change and within the extractive industry.

Prof. Muff cited to Ceres' report¹⁰ on board leadership, which recommends two inter-related approaches for weaving sustainability more deeply across board functions:

1. Integrating sustainability into board governance systems
2. Integrating sustainability into board actions.

More concretely, Ceres recommends embedding sustainability within board committees, realigning risks and incentives, increasing board diversity to include directors with sustainability expertise, focusing on long-term strategy and linking executive compensation to sustainability goals. Additionally, sustainability may be embedded in the directors' charter¹¹, employees may be recruited into designated corporate responsibility positions, and boards should emphasise long-term strategic thinking.

Shareholders' contribution to positive change:

One group suggested that companies should be required to report on responsible investments. Research has shown that socially and environmentally responsible companies have strong long-term financial performance, as measured by stock market and accounting metrics.¹²

The role of regulation:

A participant suggested that companies need a clear regulatory framework, e.g. a system for carbon pricing, and then within that regulatory framework companies should be left to adopt the corporate governance processes that best fit their needs. There was controversy about the role of companies in developing policy, with some suggesting that corporations should adopt a proactive stance in shaping the regulatory framework that they operate in to advocate for responsible regulation (rather than leaving it to those that will push for the lowest common denominator), while others argued that companies should not be politically active.

.....
Cornelio Sommaruga - former president of the ICRC

“Switzerland has a great responsibility both as the country of headquarters for humanitarian organisations as well as the home of many multinational companies. In the interests of the reputation of our country, we have to make our companies responsible too.”

Participants identified that a major challenge in this respect is that most corporations only engaged on policy issues that threaten their business model and fail to mobilise in response to problems where a solution would provide benefits to society at large, such as climate change. As a result public policy is heavily influenced by a relatively small number of companies that are interested in maintaining the status quo.

The role of corporate purpose:

Swiss law explicitly mentions shareholders only as one among other stakeholders and the responsibility of management and directors is towards the success of the company.¹³ In other words, the law does not specify that companies should maximise shareholder value. The purpose of the corporation as such is not completely determined by law and companies have significant latitude to choose their priorities.¹⁴

It was suggested by one participant that corporate purpose need not be specified by legislation as it can be different for each company. In practice, however, corporate purpose is often dictated by the shareholders of public companies. It was put forward for reflection that other stakeholders should potentially be involved in the definition of purpose. It was asked how corporate governance affects who decides on corporate purpose and whether that could be changed. One participant suggested that the understanding of the responsibility

of the board of directors could be expanded by nominating non-executive directors representing interests of stakeholders other than shareholders.

The role of shareholders and other stakeholders:

It was noted that other shareholders can serve as potential allies in the movement towards sustainability provided that they are convinced of such a shift eventually creates value.

In this context, it was noted that the Swiss legal system protects the controlling shareholders. One participant suggested that the potential positive impact of corporate governance and stewardship codes should be explored, in particular with respect to escalating beneficial shareholder engagement. Another suggestion focused on methods of organising investor pressure, e.g. the Carbon Disclosure Project.¹⁵ Additionally, positive publicity may create an incentive to buy in if sympathetic journalists and media publish information about leading companies. Participants agreed that there is a lack of information available to individual investors regarding socially responsible and impact investing, which presents a major barrier to engaging and empowering end beneficiaries. This problem may be tackled through mandating environmental, social and governance (ESG) reporting.

A participant asked whether capitalism dictates that all corporations be shareholder value maximisers. One discussant noted that at the alternative bank where he works, profit is not the purpose of the institution and therefore it is recognised that the aim is to cover the cost of capital and achieve sustainable returns. He suggested that the maximisation of profits is the problem and that limiting profitability would ease pressure on companies. Another participant argued that capitalism is compatible with various types of corporate goals and has for most of its existence led to companies pursuing goals such as market share, maximising size, diversification, rather than maximising certain accounting measures focused on shareholder wealth.

The grocery chain Migros has the flexibility to exceed minimum legal expectations for social and environmental performance because it is a cooperative, not a publicly traded company. At the same time, it must compete with Coop and other large corporations and therefore faces economic pressure to maintain its market position. As a result, the legal form may not be the most important factor determining sustainability. Another participant suggested that we should distinguish between public and private organisations - according to this thinking, it does not matter whether the company is publicly traded or not but whether it is forced to respond to expectations and pressure from diverse stakeholders.

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[Swissholding, CSR from a Business Perspective¹⁶ - 19 June 2015, p. 4](#)

“For only companies that are competitive and successful in fact meet the requirements to assume their social responsibility in the long term. At the same time CSR is in the company’s own best interest. Only those who live and respect the principle of sustainability can ensure lasting economic success.”

Leaving behind the business case for sustainability:

There was debate whether the business case for responsible corporate behaviour should be further strengthened. It was suggested by one group that there is no clear ‘win-win’ for sustainability as it requires difficult choices, conflicts of interests and power struggles. If profit is the only or primary goal, there will be problems addressing trade-offs as the interests of shareholders often conflict with those of other stakeholders, at least in the short-run. Furthermore, the business case logic may motivate greenwashing, as evidenced by the case of Volkswagen. Therefore it was suggested that a more comprehensive business case should not be developed but rather companies should work to change corporate culture and values and use them proactively.

Participants also suggested aligning management incentives to improved environmental and social performance

to increase accountability for sustainability, which would require the corporation to define relevant strategic targets. Addressing the end beneficiaries' dilemma, one participant suggested that companies may be requested to ask their employees how they would want to invest their pension contribution. Provided that pension funds offer different investment strategies with respect to sustainability considerations, this may provide a strong momentum to reshape the availability of financial capital to public companies.

Future Scenario Exercise, facilitated by Paige Morrow, Frank Bold¹⁷

Participants divided into groups that were assigned roles as different stakeholders of the corporation. Their task was to identify a potential corporate governance related innovation that their group could implement in a horizon of 5-10 years. The groups discussed the innovation as well as how to make it happen in practice.¹⁸

Institutional investors tackle carbon footprint:

A group representing institutional investors decided to address climate change. They debated whether to divest before eventually deciding that it was better to actively engage with the target company. They discussed whether they were in a difficult legal position if there was only a risk without evidence of material damage caused by climate change and noted that pension funds face a conflict between long-term interests and the short-term performance measurement that is standard within the industry. Furthermore, it was unclear how to measure carbon footprints.

With these caveats in mind, the group decided to convene a loose coalition of large investors for a carbon disclosure project that would evaluate and publish a list of the best companies and those that refused to respond to inquiries. These investors also pushed the Swiss government to commit at the Paris Climate Summit to a CO2 reduction target. The investors jointly announced that they engaged for the climate.

The pension funds then created an annual award ceremony that in its first year would publish a list of the best performing companies, before proceeding in its second year to publish a list of companies that performed poorly. The worst performers would be threatened with divestment, which would be done in the project's third year if those companies failed to improve their environmental performance.

Incentive schemes:

The group representing senior management designed an incentive scheme that could be implemented at all levels of management. Such a scheme would have to be based on a clearly defined set of long-term sustainable value goals. In other words, it must be linked to the corporation's strategic plan that integrates sustainability in the business model. All of this has to be supported by appropriate metrics.

The incentives should encourage addressing problems rather than hiding them. For example, in case of environmental damage the emphasis should be put on investigation of the cause. The incentive scheme should be intertwined with employee engagement in solving the sustainability challenges connected to company's business. Managers as well as other employees should cooperate on embedding and operationalizing values.

The company may be criticized by analysts and that may lead to a drop of stock price. To manage this risk, the company could actively seek new, patient investors who are sympathetic to the objectives pursued by the company. This will in turn require setting an appropriate reporting system that explains how the new scheme contributes to value creation. It may be built, for example, on the use of integrated reporting. The relationship with long-term sustainability-oriented investors could be further enhanced by preferential shares. The company could also harness benefits gained from publicity. In the mid-term, the company should aim to score high on a sustainability index, if available.

Diverse Boards of Directors:

The group representing boards of directors discussed the issue of diversity. The first requirement for a successful board is that board members should collectively have the experience and expertise necessary to direct the company, including expertise in sustainability.

At the moment in Switzerland boards are very homogenous : they are composed of a majority of men, aged between 50 years and 70 years, who have similar experiences and backgrounds, mainly as finance officers, legal experts or CEOs. A proposal to include a 30% quota of women on a comply or explain basis in the revision of Swiss company law is currently being intensively debated.

The business lobby opposes this measure. For members of this discussion group, the membership of boards should be much more diverse in terms of age, gender, experience, knowledge and - in the case of multinational companies – nationality. In order to increase corporate sustainability there needs to be a human rights and environment specialist within the board, as well as a specialist on other issues. The role of the Chair is equally important; they must be able to lead a diversified group and listen to diverse points of views.

One participant provided further reflection on representation of a wider set of stakeholders in the Board or AGM. Board representation of stakeholders already exists, for example in Germany where there is compulsory employee representation on the supervisory board and traditionally banks - as lenders, shareholders, and financial advisers of companies - are also present on boards.

This type of representation is not without problems. It may ensure protection of the interests of a relatively narrow set of stakeholders but it does not guarantee sustainability. Furthermore, it might make firm-level decisionmaking more cumbersome and less efficient in proportion to the diversity of stakeholders and potentially contradictory interests included.

Regulators:

The respective group mainly discussed the basic principles government should employ in its regulatory approach. The group thus identified the following three principles:

First, government should make sure that its regulative approach does not put too many extra-pressures on corporations (which are already under considerable pressure due to the current economic situation in Switzerland). This involves making clever decisions as to which regulatory interventions bear the greatest potential in making corporations more sustainable, whilst simultaneously not encroaching on their competitiveness.

Second, government should also make sure that its regulatory interventions are harmonized both with existing national and international regulations, so that no unnecessary doublings and redundancies do occur.

And third, regulations should be flexible enough to account for differences in corporations' size, sector or industry of operation, legal form, etc.

At the roundtable and in follow-up reflections, participants explored several options for regulatory intervention. One possibility suggested by one of the participants would be to limit pension funds investments in terms of sustainability of assets, rather than asset classes. The participants discussed also how to limit capital market pressures on companies. A very radical suggestion would be to legally limit corporate profitability. While not a sufficient condition for sustainability, it might be eventually a necessary one, in the sense that it would ease market pressure on firms. The limit could be discussed and defined in terms of the 'doughnut model', i.e. a model that links profitability to the concept of planetary boundaries.

Restricting advertising to products that meet sustainability standard:

The group representing external stakeholders suggested that we should adopt a measurable scale of sustainability and use it to rank companies or financial products according to their positive contributions to society.

It would also be advantageous to restructure accounting systems to better reflect the sustainable value of a corporation in its balance sheet.

Plenary session moderated by Barbara Dubach, Engageability¹⁹

A recurring idea in the debate was the need for activism by diverse corporate governance actors. It was further suggested that in order to drive change within Switzerland, we need to change management and boards to increase diversity. In order to achieve that, we need to convince investors (especially ethical investors / SRIs) to support this change and the processes needed to get there. The traditional way of understanding profitability is out of date and needs to be expanded beyond economic risk and return to encompass social and environmental risk and return.

While there needs to be multiple responses to the looming crisis, it is necessary to identify the most significant leverage points for change, and especially those actors who have the market power needed to mainstream transformative ideas, such as pension funds. Regulation will likely be needed to guide the behaviour of laggards, such as certain small and medium companies. Leading by example is good but the question is how long it will take to achieve transformative change if we rely exclusively on a voluntary approach. Existing shareholders and boards often represent an obstacle to this change and it is unclear how to convince them or whether this is feasible.

The change-making strategy must engage mainstream corporations and present a realistic pathway for large multinational enterprises. It is important to engage the public in the debate. The corporations will not adjust if there is not a strong and broad public demand. Those who lead the change in the business world should therefore address their message to the public as well as to business insiders. The role of shareholders should not be underestimated. Given their position and influence in the present model of corporate governance, companies cannot change if they would resist it. One way to change shareholders behaviour would be to mobilise end beneficiaries. The key question in that respect is how we can educate people and create options for their engagement.

One participant suggested that it would be important to identify and present best practice examples to demonstrate that change is realistic and how it can be implemented. Another participant suggested that we should explore how to harness the synergies between different actors ranging from civil society representatives to investors to business leaders.

Concluding remarks by Florian Wettstein, University of St. Gallen²⁰

Prof. Wettstein concluded the event by suggesting that we need to move beyond the discussion about sustainability as a win-win for business and external stakeholders and recognise the need to challenge the dominant business paradigm. He contended that the focus on the business case for sustainability was useful to achieve a certain level of sustainability but has limitations. Notably, sustainability has not been empirically proven to result in improved financial returns in all cases. Additionally, it is impossible to address the question of conflicting interests within the win-win paradigm as it does not instruct us on how to address these conflicts

when they arise. The real challenge is to move beyond the business case and for that we need to change values and incentives.

References

- 1 The Modern Corporation Project is lead by Prof. Hugh Willmott and Dr. Jeroen Veldman. Jeroen Veldman is Senior Research Fellow at Cass Business School, City University, London. He has held appointments at Cardiff Business School, the Utrecht School of Governance, Utrecht University and a visiting professorship at UPMF, Grenoble. His research addresses the historical development of the public limited liability corporate form and its current status in and between organization studies, management, company law, economics, finance, accounting, politics, and corporate governance.
Hugh Willmott is Professor of Management at Cass Business School, City University, London and Research Professor in Organization Studies, Cardiff Business School, UK. He has held visiting professors at Copenhagen Business School and the Universities of Uppsala, Lund, Innsbruck, Sydney and the University of Technology, Sydney. He previously held professorial appointments at the UMIST (now Manchester Business School) and Cambridge. He co-founded the International Labour Process Conference and the International Critical Management Studies Conference.
- 2 Filip Gregor is Head of the Responsible Companies Section at Frank Bold. Since 2007 he has represented Frank Bold in the Steering Group of the European Coalition for Corporate Justice where he has coordinated global research projects focused on policy and regulatory framework for global business operations. He is also a member of the Eminent Persons Group overseeing the Human Rights Reporting and Assurance Frameworks Initiative organised by the Shift Project and Mazars.
- 3 Christine Kaufmann is a Professor of international and constitutional law at the University of Zurich Law School. Before joining the law faculty in Zurich, Ms. Kaufmann worked in the legal department and then as Director of Human Resources at the Swiss Central Bank. Later she served as Director of Legal Research and as member of the board at the World Trade Institute (WTI) in Bern. In 2013 she was appointed co-president of the newly set-up Federal Advisory Committee of the National Contact Point for the OECD Guidelines for Multinational Enterprises. Ms. Kaufmann's main research interests include the interactions between human rights and business, the relationship between the international trade and the international financial system as well as the related implications on global governance.
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- 7 Christopher Wasserman is President and co-founder of the Foundation Ecophilos as well as the Zermatt Summit Foundation, a catalyst designed for business leaders to spark inspiration, share innovation and translate into action new business development models that promote human dignity in our globalized world. He is also founder and President of the TeroLab Surface Group based in Lausanne (Switzerland). He holds a MBA from New York University/USA.
- 8 Katrin Muff is Dean of Business School Lausanne (BSL) and Program Director of the DBA, Diploma in Sustainable Business and MBA & EMBA in Sustainable Business programs. Katrin worked nearly a decade for ALCOA in different countries and holding various positions. She assumed after the position of Director, Strategic Planning EMEA of IAMS Pet Food in the Netherlands. Prior to joining BSL, Katrin co-founded Yupango, an independent coaching consultancy dedicated to developing start-up companies and training management teams.
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- 15 The Carbon Disclosure Project promotes the disclosure of greenhouse gas emissions by major corporations, in coordination with shareholders and companies.
- 16 http://www.swissholdings.ch/fileadmin/kundendaten/Dokumente/Archiv_Publikationen-Studie/Corporate_Social_Responsibility_from_a_Business_Perspective.pdf
- 17 Paige Morrow is Head of Brussels Operations at Frank Bold, where she specialises in corporate governance and company law. Paige is a Canadian-qualified lawyer who advised clients and litigated human rights, employment and commercial law matters for several years at McCarthy Tétrault LLP. She has also held positions at the Centre for the Study of Human Rights at the London School of Economics and Political Science (LSE), the Kenya National Commission for Human Rights and the South African Legal Resources Centre.
- 18 Based on a backcasting strategy process developed by the Drucker Institute (www.druckerinstitute.com).
- 19 Barbara Dubach is Founder and managing director of engageability. Barbara worked for Holcim during 13 years in different functions in Switzerland and abroad. Between 2003 and 2010, she was Senior Vice President of the Holcim Group. In 2010, Barbara founded engageability, providing advice to profit and non-profit organizations in the area of sustainable development and stakeholder engagement. She holds a PhD on "Managing Environmental Communication in Multinational Companies" at the University of St. Gallen.
- 20 Florian Wettstein is Professor of Business Ethics and Director of the Institute for Business Ethics at University of St. Gallen. Florian held various positions at Boston College, Massachusetts Institute of Technology, York University (Toronto) and University of St. Thomas in the Twin Cities (Minneapolis/ St. Paul). He is also a member of the executive committee of the International Society of Business, Economics, and Ethics (ISBEE).



Nyenrode Business University and Frank Bold¹ partnered to bring together experts from business, academia, regulators and civil society to discuss the future of big business. The roundtable event held under Chatham House Rule was part of a global roundtable series with previous events held in London, New York and Zurich and further events planned in France, Germany, Norway and Belgium. This summary captures the avenues of discussion that seemed to resonate with participants and does not exhaustively capture everything that was said.

Introduction, Tineke Lambooy, Nyenrode Business University²

The two primary objectives of the meeting were:

1. to analyse corporate purpose and how Dutch corporate governance facilitates or blocks responsible business; and
2. review the new draft Dutch Corporate Governance Code³ and comment on how it could be strengthened.

The results of the discussion on the draft Corporate Governance Code were translated into concrete amendments to the text, which are appended to this report.

Introduction, Filip Gregor, Frank Bold⁴

Henry Mintzberg, a leading management thinker, recently asked ‘do we really need stock markets?’⁵ He contrasted the entrepreneurial spirit and sense of purpose present in new companies with the pressure of capital markets to think in one-dimensional terms, namely by maximizing short-term share price. He calls this pathological, saying: “One-dimensional corporations, like one-dimensional people, are pathological: they are an invasive species that have no business in a healthy society. Why build compelling enterprises and then jettison their engagement? What kind of a society, let alone economy, does that render?”

Mintzberg’s advice to companies is to: (1) seek patient capital, (2) create a trust relationship with shareholders by issuing different classes of voting rights, and (3) protect their business model and purpose by certifying as a B corporation or by changing the business model to a cooperative. His concern about the short-termism of capital markets is shared by a number of thought leaders.

Plenary debate on corporate purpose – Moderated by Herman Mulder, Nyenrode Business University, Global Reporting Initiative (GRI)⁶

Our understanding of good corporate governance needs to look beyond business as usual to consider two additional dimensions of the responsibility of the enterprise: the length of its entire value chain and its role in (adverse) impacts on society (i.e. beyond specific stakeholder groups).

Boards must consider risks in their entire value and supply chains, not just tier-one suppliers. For example, the board of a Dutch textile company involved in the collapse of the Bangladeshi garment factory at Rana Plaza needed to ask itself whether it was aware of the deficiencies, whether it was exposed to liabilities and how it should act going forward. The future of law is forward-looking to avoid and mitigate risk.

It has been confirmed that the OECD's *Guidelines for Multinational Enterprises* apply to fund managers and minority shareholders, in addition to companies and investors.⁷ The OECD's complaint resolution mechanism has explored the extent to which institutional investors as minority shareholders have a responsibility to pressure investee companies to improve their human rights performance, or to divest.

Corporate governance is concerned with power relationships and the ability of groups to have a voice. While the Netherlands is well-known for its stakeholder model of corporate governance, it currently excludes the environment. Furthermore, there tends to be an excessive focus on risk management at the expense of innovation. We should look at examples where strong corporate governance has been embedded throughout the organisation, for example in B Corporations.⁸

One participant suggested that the objective of corporate governance should be to realise the purpose of the corporation and put incentives in place to achieve those ends. Others questioned the extent to which we can legislate for purpose. One participant also noted the distinction between purpose and consequence. Everyone agreed that companies should avoid causing bad consequences. It is however unclear whether the creation of beneficial societal outcomes is part of the corporation's purpose under the liberal market model. It may be that the question of purpose is bigger than can be solved by corporate governance. Furthermore, it may be misleading to speak about a corporation as having one single purpose. While this might be true of small companies, large corporations have diverse products and therefore have multiple objectives.

The debate about purpose is cyclical and we should therefore review existing literature on the legal debate about the 'corporation in itself' ('Unternehmen an sich') to build on what we already know. It was suggested that the main problem with a corporate purpose that espouses the creation of beneficial societal outcomes is that it allows managers to play different stakeholder interests against each other, which allows them to justify virtually any course of action or decision. A broad definition of corporate purpose must therefore be coupled with a strong managerial ethic. Indeed, virtuous managerial behaviour (Beamtenidealismus) - rather than selfish maximisation of personal wealth - was the fundamental assumption of the 'Unternehmen an sich' view in Germany and Switzerland during the 1920s and 1930s. Yet it may be that we should not return to these former understandings of the role of business in society but rather evolve to a new one.

Another participant thought that the question of corporate purpose reflected a shareholder model thinking frame. Since the Netherlands uses a stakeholder model, a company's purpose is/should be the outcome of the interests of all stakeholders. Similarly, Dutch politics are carried out within a coalition-consensus model.⁹ The question then becomes in what forum should this weighing of interests be carried out; one idea that resonated was the use of stakeholder fora/assemblies.

The analogy has been used of corporate profit being akin to red blood cells, in that it is needed for survival, but the generation of profit is no more the purpose of the corporation than the generation of red blood cells are the purpose of human existence.¹⁰

In the 1990s, the key issues in corporate governance tended to be a formalistic discussion of the importance of the supervisory role of non-executive directors (NEDs), the topic of board composition, etc. while now it is recognised that culture and leadership play a crucial role in companies. Most seem to agree that the maximisation of shareholder value cannot be the only answer to the question of corporate governance. More recently, there has been a trend back from rule-based regulation to a principle-based approach.¹¹

Martin Luther King said that “morality cannot be legislated, but behaviour can be regulated.”¹² We have witnessed an enormous loss of public trust in business, as well as a in civil leaders, due to failure to adequately regulate behaviour. The effects of this are potentially destabilising as they risk creating a power vacuum.¹³

One way to introduce checks and balances internally to prevent serious scandals would be to require boards to conduct an effective and systematic internal investigation in response to complaints of wrongdoing. Where companies have adopted ethical codes (gedragcodes) they should be adhered to. When a violations of either an internal code or the Corporate Governance Code is reported to the board of directors, they should seriously investigate the reported incident and ensure appropriate correction - and where relevant take appropriate action to manage the consequences.

Scenario Exercise – Paige Morrow, Frank Bold¹⁴

Participants engaged in a backcasting exercise where they were asked to design a corporate governance innovation to address a challenge facing a mock company.¹⁵ Each group was asked to assume a different position (board of directors, management, employees, accountants and institutional investors) and then develop a corporate governance innovation that could be implemented in the next five years.

Board of directors

The group of directors said that it was important to develop a clear mission. Currently boards have too many functions and goals, and there is a lack of distinction between the roles of executives and non-executives. The board should have a clear separation of responsibilities and aim at ensuring the long-term continuity of the firm.

Management

The group representing management discussed the creation of a matrix measuring the net positive impact value (NPIV) of business decisions to shareholders, stakeholders and society-at-large, and their alignment with the corporation’s purpose. The matrix could be updated every 1.5 years. This would help the business to accomplish the following:

1. Establish a clear purpose, vision and strategy for the company;
2. Test their ability to make decisions in accordance with the purpose;
3. Build in flexibility to change the indicators but retain the corporate culture to take decisions that are fully in accordance with the corporate purpose.

The group felt that this innovation would improve the decision-making processes of organisations and increase the consistency of business decisions that are sustainable and mission-driven. It would also build trust both within the company and with its external stakeholders. Here it is interesting to look at B Corporation requirements for corporate governance and decision-making.¹⁶

Employees

The employee group discussed the role of labour and agreed that board-level representation is important. The group explored the idea of creating a ‘shadow board’ of employees. The group also discussed a potential cap on the ratio between that of the CEO and lowest paid worker, which was unsuccessfully put to a Swiss referendum in 2013.¹⁷

Accountants

The group of accountants discussed bringing civil society input to the board of directors and the CEO through additional non-financial reporting based on materiality.¹⁸ It is important for this information to be comparable with like information from peers. This innovation would have the benefit of future-proofing firms' value creation and bringing civil society input into businesses in a constructive way. Through the introduction of a self-assessment process and auditing process, the Board's ability to select and define goals and KPIs that represent all legitimate stakeholders' interests would be strengthened.

Institutional investors

It was suggested that every company should develop a statement of purpose at the time of incorporation. This would be revisited at annual stakeholder meetings, which resemble annual general meetings with the additional of stakeholders. This would allow companies and stakeholders to arrive at a shared understanding of corporate purpose.

Additionally, institutional investors should be required to prepare integrated reporting¹⁹ from the perspective of managing the expectations and interests of end beneficiaries, and should also require investee companies to adopt integrated reporting. One example is Unilever, which prepares a statement where they explain why they are on this earth for all stakeholders; however, one participant noted that it was uncertain what the role of the corporation was in this regard.

Discussion of Dutch Corporate Governance Code

Irene Heemskerk, member of the Dutch Monitoring Committee Secretariat,²⁰ presented the Committee's proposal to revise the Dutch Corporate Governance and explained certain additions and changes. She emphasised that the application of the Code is limited to Dutch listed companies. The Code is focused on responsibility and transparency. Adherence is on an 'apply or explain basis' (a variation on the comply or explain principle typical to corporate governance) and reporting on compliance should be appended to the annual report. An interesting feature is the use of best practices – 129 in all – to provide concrete guidance to companies on how to implement their obligations under the Code.

The 2016 revision aims to address a number of matters:

1. Increased focus on long-term value creation;
2. Reinforcement of risk management;
3. New emphasis on effective management and supervision;
4. Introduction of culture as an explicit element of corporate governance;
5. Clarification and simplification of the rules on the remuneration;
6. Revisiting the relationship with shareholders and stakeholders; and
7. Clarification of requirements regarding the quality of explanations.

Participants then divided into working groups to analyse and provide concrete suggestions for principles that were relevant to the roundtable, namely long-term value creation, non-financial risk management, and culture.

Principle 1.1 Long-Term Value Creation

Participants were positive about the inclusion of long-term value creation. They noted however that the Code does not define 'long-term' and it is left to each company to determine the relevant time horizon. It was suggested that it would be helpful to provide some guidance on the factors that should be considered.

There are two time dimensions relevant to the 'long-term'. First, there is the long-term time horizon for the company itself, which may stretch to five years or beyond. Second, there is the very long-term relating to the business' impacts and value creation for 'societal interests, such as climate change. It was suggested that the term 'societal interests' should be used as it is a broader concept than 'shareholders', 'stakeholders' or 'civil society', as currently in use in the Code. Both need to be considered.

Additionally, the value created should be for the long-term benefit of all stakeholders, including but not limited to shareholders and employees. Here it may be useful to refer to the OECD Guidelines for Multinational Enterprises, which acknowledge the importance of creating value for all stakeholders, including but not limited to shareholders.

The group further observed that changes on a very long time horizon (e.g. 50 years) are often believed to be greater than they are in practice. Conversely, and counterintuitively, changes to the company and impacts caused by the company on a mid- to long-term horizon (e.g. 5-10 years) are often under-estimated.

The idea was put forward to consult with stakeholders to create a materiality matrix to identify the most relevant issues of the company and then develop key performance indicators (KPIs) to measure progress on these key issues. Both financial and non-financial performance should be monitored and measured. Additionally values should be integrated into the KPIs. It was acknowledged that some accounting firms already use materiality matrices with their corporate clients.

Participants echoed the importance of supervisory board diversity that is emphasised in the draft Code (at p. 26 and Principle 2.1.5), in terms of multiple types of background, including gender and age. It was suggested that boards should also include young people, e.g. under 30 years of age, in order to include the (future) perspectives of the new generation in decision-making.

Principle 1.2 Risk management & Principle 1.4 Risk management accountability

There was a question about who should have the responsibility for establishing the criteria for setting the risk appetite of the company and it was felt that stakeholders should have a more prominent role in this respect.

It was suggested that there is a need for more than vague statements on long-term value creation. Companies need to think practically to identify the concrete long-term value drivers and apply those to their strategic planning. Furthermore, while risk management is important, risk aversion needs to be offset by innovation and creativity. In the current business environment, innovation is under-prioritised. One solution could be to have someone on the board responsible for innovation and creativity.

With respect to environmental, social and governance (ESG) matters, the expertise of board members should be matched with achieving ESG goals and reporting on non-financial matters. Several participants asked how ESG matters would be monitored through ongoing due diligence²¹ and reported on.

The current forward-looking approach asks for a guarantee that the company will exist in one year (in the control statement). It is unclear what this means for the liability of directors. There is a need to protect directors from the possible consequences of a future-oriented statement about being in control over the next year. It was asked whether boards should provide a vision, rather than a risk assessment.

In this context, the importance of board diversity was raised²². It was noted that a diverse board will reduce the possibility of group think and ensure there is a broad range of individuals with varying thresholds for risk.

With respect to the 'in control statement', it was argued that the current draft version of the Code is

insufficiently aligned with the long-term view espoused in the rest of the Code and frames ‘control’ too much as financial control. This is unfortunate, as there is a sense of urgency across a wide set of stakeholders, including insurance companies, the director of the Dutch Central Bank (Klaas Knot), Mark Carney, Andy Haldane, Christine Lagarde (IMF) and many others that the future liabilities of intangibles like climate change impact, loss of biodiversity and ecosystems, stranded assets, costs of conflict, reputation damage etc. should be central to the way companies think and report about risks and, hence, control.

It was suggested that the Committee may wish to give further guidance to companies. For example, companies’ risk appetite should align and refer to the stakeholder approach stipulated in Principle 1.1. Companies may achieve this by referring to social issues, human rights matters, the environment and corruption (as outlined in EU Directive 2014/95 on non-financial reporting). Companies may also choose to create a materiality matrix based on GRI G4 Aspects²³ or the International <IR> Framework²⁴ and then base their risk appetite decision-making on this.

Principle 1.3 Internal audit function

It was suggested that the option to choose not to have a voluntary internal audit committee should be explained in the Code. It was unclear in the current draft why the internal audit committee reports to the board and not to the general audit committee. Further explanation could help to show how the independence of the internal audit would be guaranteed, especially for an audience familiar with one-tier boards where the independence of the internal audit committee is expected. As it stands, the draft text could raise questions in an international context. It may be appropriate to address this issue further in the next version of the Code when the Committee focuses additional attention on the distinctions between one-tier and two-tier boards.

Principles 2.5 Culture

The 2016 Code is the first to put culture on the board’s agenda. The addition of culture as a core principle is probably the first of its kind in any corporate governance code as no other code explicitly requires boards to take responsibility for it.²⁵

Participants universally welcomed the newly introduced principle on culture, which they agreed was extremely advanced relative to other Codes. It was suggested that culture is the ‘driving force’ of the company and it is impossible to run a business without considering its values. Furthermore, accountability and openness are essential to the survival of the company because they help to gather information internally as well as on the external business environment, which is constantly evolving.

The group noted that the aims of this principle are heading in the right direction but further guidance could be given on implementation. Culture is a broad term and corporate culture is embedded in the broader culture of the country. It was unclear whether culture should align with the country culture where the company is based, and indeed this may be difficult to identify in the case of large multinationals. It was noted that the OECD Guidelines on Multinational Enterprises requires Dutch companies to apply Dutch norms everywhere they do business even if local norms are lower.²⁶

General Comments

It was noted that there is sometimes confusion about the requirements of the ‘comply or explain’ principle. Participant welcomed the clear requirement that companies give “a reasoned explanation” for any deviations from the Code,²⁷ although some asked whether at least a portion of the Code’s provisions should eventually evolve to become mandatory requirements. Additionally, several participants were troubled by the limited application of the Code to Dutch listed companies and felt that it should apply more broadly.

The question of monitoring and enforcement of the Code was raised. The proposed Code states that it is the

role of shareholders “to call the management board and the supervisory board to account for compliance with the Code” (p. 56). Shareholders share the “responsibility” with companies for “good self-regulation according to the ‘comply or explain’ principle so that it can serve as an effective alternative to legislation”.

Several participants noted that enforcement has been a weakness of the ‘comply or explain’ principle in the Netherlands and elsewhere.²⁸ It was recommended that the responsibility of monitoring and enforcing the Code should be shared with other stakeholders. One suggestion was to introduce a communication channel for stakeholders to communicate directly with companies. Other participants suggested creating an index to measure compliance with the Code, thereby creating positive incentives for compliance. This would be more constructive than ‘naming and shaming’ companies that failed to comply. The Access to Medicine Index could be an interesting example to look at as it uses a relative ranking to encourage companies to constantly seek to improve their performance relative to other businesses, rather than giving a pass/fail grade.²⁹ Additionally, a self-evaluation process could be used to create an incentive for boards to look at their implementation and create a culture of self-improvement.

It was suggested that the Code should be reviewed more regularly. It seems that this is already foreseen under the new rules for the Code.

It was also asked whether a European Corporate Governance Code was an idea that should be developed.

References

1. Frank Bold is a purpose driven law firm using the power of business and non-profit approaches to solve social and environmental problems. It leads the Purpose of the Corporation Project, a strategic and open-source platform for leading thinkers and organisations interested in promoting the long-term and sustainability of companies to share their knowledge and foster multi-stakeholder collaboration.
2. Tineke Lambooy is Professor of Corporate Law at Nyenrode Business Universiteit. She conducts multidisciplinary research projects which focus on the implementation of sustainability standards by private actors (corporate social responsibility, CSR). One special focus area concerns the participatory stakeholder model of social enterprises. Another subject of research regards natural capital and the role of business in that context. She was trained as a corporate lawyer and conducted her PhD study on the role of legal norms and corporate best practices in regard of the development of CSR standards. Tineke is a board member of the Club of Rome - Dutch Chapter and a member of the Round Table of World Connectors.
3. The unofficial English translation is available at <http://www.commissiecorporategovernance.nl/download/?id=2835>.
4. Filip Gregor is Head of the Responsible Companies Section at Frank Bold. Since 2007 he has represented Frank Bold in the Steering Group of the European Coalition for Corporate Justice where he has coordinated global research projects focused on the policy and regulatory framework for global business operations. He is also a member of the Eminent Persons Group overseeing the Human Rights Reporting and Assurance Frameworks Initiative organised by the Shift Project and Mazars.
5. Mintzberg, Henry (2016) “Do we really need stock markets?” available at www.mintzberg.org/blog/stock-market.
6. Herman Mulder is an institutional adviser, speaker, lecturer and author on sustainable finance issues. He is most notable for being an advocate, expert in international law and has been attributed to be a key player in the development of corporate responsibility, impact investment and the ESG integration. He is currently a chairman of the True Price Foundation, member of the Board of the Dutch National Contact Point for the OECD Guidelines for MNE’s, former chairman of the Global Reporting Initiative (GRI) and member of the TEEB Advisory Board. A former Director-General, Head of Group Risk Management at ABN AMRO Bank (1998-2006) and Head of Global Structured Finance (1995-1998), Herman Mulder was the initiator of the Equator Principles (2002/2003: the first voluntary, global sector code on environmental and social issues for the financial sector).
7. For example, in a complaint brought against the South Korean company POSCO and two of its investors, the

Dutch pension fund ABP and its pension administrator APG, the Dutch National Contact Point confirmed that the OECD Guidelines apply to financial institutions that have minority shares in multinational enterprises. Although ABP/APG held less than 1% stake in POSCO, they had an obligation to prevent or mitigate any violations carried out by the investee company.

8. B Corporations are companies that have been privately certified as meeting social and environmental performance standards. See Cummings, B. (2012). Benefit corporations: How to enforce a mandate to promote the public interest. *Columbia Law Review*, 578- 627 at p. 594.
9. Andeweg, R. B., & Irwin, G. A. (2014). *Governance and Politics of the Netherlands*. Palgrave Macmillan at p. 141.
10. Ed Freeman, a trustee of Conscious Capitalism Inc. said: “We need red blood cells to live (the same way a business needs profits to live), but the purpose of life is more than to make red blood cells (the same way the purpose of business is more than simply to generate profits).”
11. J. Van Bekkum, J.B.S. Hijink, M.C. Schouten and J.W. Winter, ‘Corporate Governance in the Netherlands’, 14 *Electronic Journal of Comparative Law* 3 (2010).
12. Martin Luther King, Jr., “On Being a Good Neighbor.” In *Strength to Love* (Cleveland, Ohio: William Collins, 1963), 35.
13. Edelman, 2016 Trust Barometer, available online at <http://www.edelman.com/insights/intellectual-property/2016-edelman-trust-barometer/>.
14. Paige Morrow is Head of Brussels Operations at Frank Bold, where she specialises in corporate governance and company law, and an external lecturer in corporate governance at the University of Kent BSIS. Paige is a Canadian- qualified lawyer who previously advised clients and litigated human rights, employment and commercial law matters at McCarthy Tétrault LLP. She has also held positions at the Centre for the Study of Human Rights at the London School of Economics and Political Science (LSE), the Kenya National Commission for Human Rights and the South African Legal Resources Centre.
15. Based on a scenario exercise developed by the Drucker Institute and used with its permission. For a general explanation of backcasting, see e.g. Quist, J., & Vergragt, P. (2006) ‘Past and future of backcasting: the shift to stakeholder participation and a proposal for a methodological framework’ *Futures* 38(9): 1027-1045.
16. See B Lab <<http://www.bcorporation.net/become-a-b-corp/how-to-become-a-b-corp/performance-requirements>>. For an examination of social purpose, see Lambooy, T. and Argyrou, A., *Improving the Legal Environment for Social Entrepreneurship in Europe* (April 24, 2014). *European Company Law Volume 11 Issue 2*; University of Oslo Faculty of Law Research Paper No. 2014-03. Available at SSRN: <http://ssrn.com/abstract=2428706>.
17. The Young Socialists of Switzerland collected the requisite 100,000 signatures required to trigger a referendum on the question whether CEOs’ salaries should be capped so that they would not earn more in one month than the average earned by the lowest paid worker(s) in that company in the entire year. The referendum ultimately received only 34.7% of support. See <http://www.bloomberg.com/news/articles/2013-11-24/swiss-voters-reject-strictest-executive-pay-limits> for more information.
18. In accordance with the requirements of the Non-Financial Reporting Directive and the Dutch Corporate Governance Code.
19. Including reporting on both financial and non-financial information. The International Integrated Reporting Council (IIRC) defines integrated reporting as “a process that results in communication by an organization, most visibly a periodic integrated report, about how an organization’s strategy, governance, performance, and prospects lead to the creation of value over the short, medium and long-term. See PwC (August 2013) *Integrated Reportign: Going Beyond the Financial Results*; available at <https://www.pwc.com/us/en/cfodirect/assets/pdf/point-of-view-integrated-reporting.pdf>.
20. Irene Heemskerk is Secretaris (Secretary) of the Dutch Corporate Governance Code Monitoring Committee. She prepared the proposals for revision of the Corporate Governance Code and is involved with the ongoing monitoring activities of the Committee. She started her professional career at the Ministry of Transport in The Hague, where she was trained as a legislative lawyer. Irene joined the Dutch Central Bank in 2005 and subsequently took on positions as a legal counsel, a supervisor, and senior policy advisor on integrity and governance issues in the financial sector. She was also closely involved in the parliamentary inquiry into the Financial System. In October 2014, Irene started a secondment as the Secretaris (Secretary) of the Dutch

Corporate Governance Code Monitoring Committee.

21. For example, with respect to due diligence for social impact the UN Guiding Principles on Business and Human Rights, Principle 17 states: “In order to identify, prevent, mitigate and account for how they address their adverse human rights impacts, business enterprises should carry out human rights due diligence. The process should include assessing actual and potential human rights impacts, integrating and acting upon the findings, and tracking responses as well as communicating how impacts are addressed.”
22. The Netherlands introduced legislation that requires the boards of large Dutch companies to be of at least 30% women and 30% men. However, this requirement applies on a comply or explain basis. Principle 2.1.5 of the proposed Code asks companies to explain any failure to meet the 30% target. According to the 2015 Dutch Female Board Index, only 7.8% of executive board members and 21.3% of supervisory board members are women: <https://www.tias.edu/docs/default-source/Kennisartikelen/femaleboardindex2015.pdf?sfvrsn=0>
23. The Guidelines organize indicators (or Specific Standard Disclosures) into three Categories - Economic, Environmental and Social. See Global Reporting Initiative (2014). G4 Reporting Principles and Standard Disclosures. For further reading on materiality and its application beyond financial accounting into integrated reporting, see Edgley, Carla. “A genealogy of accounting materiality.” *Critical Perspectives on Accounting* (2013).
24. The <IR> Framework uses a principle-based approach and does not prescribe specific KPIs but rather identifies the process for determining materiality. Eccles, Robert G., and Michael P. Krzus. *The integrated reporting movement: Meaning, momentum, motives, and materiality*. John Wiley & Sons, 2014, ch. 5.
25. The Draft King IV Report on Corporate Governance for South Africa 2016, which opened for public consultation on 14 March 2016, also addresses culture. The Draft King IV Report is available at <http://bit.ly/KingIVdraft>.
26. See Dutch NCP statement on the situation in the Philippines.
27. The Code sets out at p. 56 of the proposed Code the five elements that companies must give in their explanation of why a best practice principle was not applied, which are: 1. how the company departed from the best practice provision; 2. the reasons for the departure; 3. a description of how the decision to depart from the best practice provision was made within the company; 4. if the departure is of a temporary nature and continues for more than one financial year, an indication of when the company intends to comply with the best practice provision again; and 5. where applicable, a description of the alternative measure that was taken and either an explanation of how that measure attains the underlying purpose of the best practice provision or a clarification of how the measure contributes to good corporate governance of the company.
28. In the UK, compliance with the Corporate Governance Code is a requirement of the listing rules of the London Stock Exchange, albeit on a comply or explain basis. See e.g. Keay, A. (2014). *Comply or explain in corporate governance codes: in need of greater regulatory oversight?* *Legal Studies*, 34(2), 279-304.
29. The Access to Medicine Index, an independent initiative, ranks the world’s 20 largest research-based pharmaceutical companies according to their efforts to make their products more available, affordable, and accessible in developing countries. See Hogerzeil, H. V. (2013). *Big Pharma and social responsibility—the access to medicine index*. *New England Journal of Medicine*, 369(10), 896-899.
30. We recommend including in the explanatory comments that management is expected to organise a meaningful stakeholder consultation process that should be described in their reporting.
31. As a general comment that applies to all provisions and best practices, we recommend every norm be written in the current tense in order for the comply or explain mechanism to fulfill its objective. For example if the text states ‘should...’or will...’, the company can say that it complies because it will do so in the future. We noticed this occurring for the Diversity provisions in the old Code relating to board diversity. We noticed that many companies that had no diversity in place still considered themselves compliant because they had plans to comply in the future (‘will’).
32. We recommend adding into the explanatory text that management should discuss how they have consulted with stakeholders. Some companies have begun to report the stakeholders they consulted with and this may be taken as best practice in order to give investors an understanding of how meaningful the consultation process has been.
33. In the Preamble, the Commission states that it deleted the term ‘CSR’ because it is deemed to be integrated in the strategy and elsewhere. Hence, everywhere that a Principle or Best Practice uses the term ‘financial’, the words ‘and non-financial’ should be added, Thus, the Commission’s new vision should be applied consistently, Eventually,

we hope to see a complete integration of CSR into the Dutch Van Maanen Corporate Governance Code, in line with the South African Corporate Governance Code (King III).

34. We recommend that the audit committee be made explicitly responsible for the appointment of the internal auditor, or at least consent to the appointment. This responsibility should not be held by the management board alone.
35. We recommend that the term corporate report be used as it more accurately reflects the integration of both financial and non-financial information into reporting.



Co-hosted by: ACCA Global, Cass Business School and Frank Bold

Frank Bold, with the support of ACCA (the Association of Chartered Certified Accountants), organised a roundtable on responsible investment and reporting. The event was particularly relevant in view of the two current consultations published by the European Commission on non-financial reporting and long-term and sustainable investment. The consultations served as a basis for the debate on EU policy developments and the role of business, investors and civil society in fostering a sustainable economy and responsible business behaviour.

The roundtable was composed of two panels of speakers followed by discussion under Chatham House Rule:

- Will Martindale, Head of Policy at UN Principles for Responsible Investment
- Zsofia Kerecsen, Policy Officer, DG Justice, European Commission
- Flavia Micilotta, Executive Director, EUROSIF
- Ophélie Mortier, Responsible Investment Strategist, Degroof Petercam)
- Nicolas Bernier-Abad, Policy Officer, DG FISMA, European Commission
- Richard Martin, Head of Corporate Reporting, ACCA
- Michel Bande, Senior Executive Vice President, Solvay
- Jeremy Nicholls, CEO Social Value International and Social Value UK

Moderators: Paige Morrow, Head of Frank Bold Brussels operations and Filip Gregor, Head of Responsible Companies Section at Frank Bold

Main Highlights:

Will Martindale, UN Principles for Responsible Investment

In his introductory remarks, Will Martindale, Head of Policy at [UN Principles for Responsible Investment](#), focused on how asset owners can drive responsible investment and the issue of fiduciary duties.

Asset owners

Even though many asset owners have made commitments to responsible investment, the majority have yet to ensure that these are effectively implemented. Issues include:

- Inconsistencies in investment practices in different asset classes
- High-level statements on sustainability or environmental, social and governance issues are often missing from investment beliefs
- Responsible investment commitments are not embedded in investment mandates

By implementing their commitments to responsible investment with sufficient scale and depth, asset owners can accelerate the development of responsible investment throughout the investment chain.

The weaknesses in asset owner implementation and the consequent effects on investment manager behaviour also affect the relationship between investors and policy makers. UN research indicates that many policy

makers are sceptical about investors' motivations; they see piecemeal implementation of responsible investment as indicative of a deeper lack of commitment to responsible investment and sustainability.

Will identified five distinct barriers to asset owners taking a more proactive approach to responsible investment:

- The perception that ESG issues do not add value to investment decision-making
- The perception that significant additional resources are required to implement responsible investment
- The perception that investor duties, and in particular, fiduciary duty, prevent investors from taking a proactive approach to responsible investment
- The advice given by investment consultants, which is often seen as not supporting proactive approaches to responsible investment
- The products provided by investment managers, which often do not meet the responsible investment needs of asset owners

Therefore, the UNPRI recommends six steps for asset owners in order to drive responsible investment:

- Understand the investment environment
- Define investment goals
- Define investment beliefs
- Establish investment governance processes
- Formulate investment mandates
- Monitor, review and report

Finally, Will called for active engagement of investors in policy making processes, which he distinguished from political lobbying. There is still much scepticism about the effectiveness of policy engagement and a lack of understanding regarding how to influence policy processes.

Fiduciary duties

UNPRI report 'Fiduciary duties in the 21st century' concludes that fiduciary duties (or equivalent obligations) exist to ensure that those who manage other people's money act in the interests of beneficiaries, rather than serving their own interests. The purpose of the report is to end the debate about whether fiduciary duty is a legitimate barrier to investors integrating environmental, social and governance (ESG) issues into their investment processes. Key findings show that failing to consider long-term investment value drivers (including ESG matters) in investment practice is a failure of fiduciary duty. Despite significant progress, many investors have yet to fully integrate ESG issues into their investment decision making processes.

Reports references:

[How Asset Owners Can Drive Responsible Investment \(PRI\)](#)

[Fiduciary Duty in the 21st Century \(PRI, UNEP FI, UNEP Inquiry and UN Global Compact\)](#)

[The Case for Investor Engagement in Public Policy \(PRI\)](#)

.....
David Pitt-Watson, UNEP Finance Initiative

"It must be about working together to be sure that our industry serves its clients and can deliver on its purpose of providing the capital which will deliver long-term prosperity"

.....
Professor Paul Watchman, University of Glasgow

"The concept of fiduciary duty is organic, not static. It will continue to evolve as society changes, not least in response to the urgent need for us to move towards an environmentally, economically and socially sustainable financial system"

First panel: Long-term and sustainable investment

The public consultation on long-term and sustainable investment was launched in December 2015 and closed on 25 March. The issue has launched a big debate but there is little indication what the outcome of the consultation will be. The Commission will issue a feedback statement and then will start discussions on further actions.

It was mentioned that Europe needs significant new long-term sustainable investment to maintain and extend its competitiveness. The issue is not new, as the European Commission has already been working in this area, for example on the revision of the Shareholder Rights Directive.

It was also suggested that the current Capital Markets Union Action Plan works to foster long-term sustainable investment and achieve EU policy objectives, specifically those linked to climate change and resource efficient economy.

Relevant and reliable information disclosure

A panelist highlighted that companies are not the sole player when it comes to providing information, as there are also ratings agencies, financial advisers and traders. This can generate confusion as regards to which is the most crucial information.

It was underlined that, for investors, quality of information and transparency is key. Investors want to collaborate with ESG rating agencies although it does not help that they often have different methodologies which results in very diverse kinds of information. Companies are also screened and rated according to different criteria. These comments led to the conclusion that investors want to have a clear view on how to assess industries and how to assess ESG issues. A more prescriptive approach is needed and investors need easier access to information in order to have more clarity when making investment decisions. It was also noted that we should not make a distinction between stakeholders and investors.

Some speakers noted the importance of taking a comprehensive approach – defining what measures and data are material. Reporting must be material so we are able to use this information. This prompted the debate on how materiality is defined and to what it applies.

In terms of quantity, investors do not need too much data; instead they need data that can be used. Disclosure does not necessarily mean transparency. A concern was raised over the inclusion of SMEs in regulation, as large companies have more resources to disclose the necessary data, and they could apparently seem to be more transparent than other companies.

It was also suggested that a clearer definition of responsible investment is needed.

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Paige Morrow, Frank Bold

“It is increasingly clear that sustainability and responsible business behaviour go hand in hand with prosperity and strong markets. If societies or the environment fail, so will financial markets”

Environmental and Social Issues

We cannot run businesses like before - It is important to integrate social and environmental matters. It was stated that companies with improved non-financial performance will outperform their competitors in the medium and long-term. A remaining challenge is that financial markets remain focused on the short-term, and it is not easy to reconcile long-term value creation with shareholder pressure.

More emphasis needs to be put on education and training – we operate with more data that is becoming more

complex and there aren't enough experts to work with it. Standards are increasing but we need also increasing expertise from the auditors and from the compliance and monitors services.

Second panel: Non-financial reporting guidance

The public consultation on the non-financial reporting (NFR) guidelines was published on 15 January 2016 and will be open until 15 April 2016. The speakers on the second half of the roundtable focused on this directive and debated the issues of materiality, concrete requirements/indicators for NFR disclosure, assurance as well as integration and strategy.

Corporate purpose, sustainability, and governance

The moderator and host of the event, Filip Gregor, stated that the reporting framework is fairly well developed to protect shareholders from financial mismanagement. However, it does not show other important matters that are key to corporate success, including culture, ability to innovate, management qualities, other intangible assets, long-term risks, and associated strategies. Connected but sometimes separate is the understanding of what role the corporations play in societal and environmental risks, some of which may be risks to companies and some may be systemic, endangering markets, society, or the environment that are corporations' life support.

Investors play an important role in corporate governance, but in leading companies the primary users of the "non-financial" information are the senior management. It was then stressed that people and systems have a tendency to manage what gets measured, but we must not forget there is a complex system that influence corporate decisions. Where possible, the non-financial reporting framework should provide clear indicators and methodology for specific matters. For some matters it is easier than for others. In general, a company's reporting should produce information enabling to understand the business' strategy. These two perspectives are not contradictory.

Key issues for the NFR guidelines

A statement was made affirming that Europe has taken a big step forward in non-financial reporting aspects and has introduced a system that can be considered unique in the world. It is an horizontal legislation that applies to large companies in all sectors, which involves around 6,000 businesses.

The European Union is determined to make the transparency of large companies part of the solution. Along these lines, it was mentioned that this directive is supposed to push companies to act more responsibly. Importance, compliance with the directive will not be based on the comply or explain principle, as we are accustomed to in corporate governance.

One speaker affirmed that under the EU accounting directive as amended by the new NFR directive companies have an obligation to disclose information that is relevant for understanding their business and the impact of their activities. The Commission is undertaking a consultation process that will result in non-binding guidelines on the methodology for non-financial reporting, and this will neither be a detailed nor long document.

It was also stated that we need to think big about the consultation and aim at good deliverables. The guidelines will not be an operational document; it most probably will not be a "how to" document, but rather an inspirational one. The debate on what is 'material' was brought up again by one of the speakers who specified that EU legislation has already defined materiality – article 19 of the Accounting directive – which includes content and impact of the activity.

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Filip Gregor, Frank Bold

"Non-financial reporting is a tool; it must be integrated in decision and strategy making as well as in the overall corporate governance framework"

Main challenges and opportunities for improving NFR framework and practice in the long-term

Richard Martin, ACCA

Companies need to integrate transparency requirements into their strategies, and link them with their financial and non-financial performance indicators

Some speakers stressed that information needs to be comparable while others disagreed and pointed out that comparability is a secondary objective. One of the issues raised in this respect is that investors need to know that the information has a level of standardisation that permits comparability, not of the things in it, but the process and decision-making that led to it.

There were also some doubts expressed about the scope of the directive and the success of it in improving transparency: “are we reaching enough of the European economy by targeting the biggest corporations?” It was then stated that this directive can be seen as a first step, but we need to ensure that the result of it will be high quality reporting.

Another issue debated was that a lot is left to member states to expand. As for all directives, this is considered a sort of minimum, a benchmark to which member states can add. But it was pointed out that member states may impose very different requirements on specific issues, such as the degree of assurance provided for non-financial information.

One speaker hoped that companies will use the transparency requirements to integrate some of these issues into their strategies. If not, the risk is that this will become a list of things that people have to report on but the quality of that list may not be poor and the relevance to the individual corporation may be low.

In the discussion, it was also mentioned that there is a danger of people perceiving the production of non-financial information as a burden or cost. We need to work with companies that stand up and recognise that high-quality non-financial information is useful to drive their financial decisions - the two types of information should be seen as complementary.

Lastly, it was mentioned that the legislation has not determined the audience for non-financial statements, and this might be problematic. The current reporting framework primarily relies on investors to monitor and enforce the quality of disclosure, whereas non-financial disclosure is arguably for a broader set of stakeholders. It is not clear that mainstream investors are currently able or willing to assess the quality of non-financial reporting, and conversely there is no mechanism for civil society organisations or other stakeholders to enforce these rules.

 Frank Bold

Think Ahead



Cass Business School
CITY UNIVERSITY LONDON

Co-hosted by: Affectio Mutandi and Cass Business School and Frank Bold

Frank Bold organised a roundtable on corporate governance in Paris with Affectio Mutandi and Cass Business School. Building on previous events held in London, New York, Zurich, and Breukelen (the Netherlands), the discussion in Paris focused on corporate purpose and the creation of long-term sustainable value. Keynote speeches were given by Professor Alexis Constantin (Université de Versailles Saint-Quentin) and Thierry Philipponnat (Institut Friedland, Forum pour l'Investissement Responsable, French Financial Markets Regulator (l'autorité des marchés français, AMF) and formerly of Finance Watch).

Alexis Constantin

Alexis Constantin suggested that corporate governance does not have any legal meaning in France, although the term is found in several fields of law. It seems nevertheless accepted that the corporate governance model must be developed according to an objective specific to the governed entity. This has been extremely complicated to achieve since the notion of the company (legal form) has become maladapted to the concept of the business (meaning its activity).

In fact, a company is defined as the 'thing' that belongs to shareholders while the notion of business encompasses a plurality of actors, i.e. stakeholders that are both internal and external to the company, including commercial partners, creditors and employees. The concept of the 'company' only refers to the legal structure of a corporation while the notion of the business, which includes stakeholders, matters much more in practice due to the growing influence of several external stakeholders

We are today witnessing a breakdown of the concepts of the company and its shareholders and by extension of corporate law as well. Article [1832](#) of the Civil Code provides that 'a company is created by two or several persons who agree by a contract to appropriate property or their industry for a common venture with a view to sharing the benefit or profiting from the saving which may result therefrom'.

Thus, the current French concept of social interest appears as a closed and residual notion, which is more focused on profit than the Anglo-Saxon version. It is time to adapt it to what really matters, i.e. social interest, and to hence include in its definition the respect of social and environmental aspects. This would actually amount to a simple adaptation of Article [1382](#) to the rest of French law, as corporate obligations to avoid social and environmental impacts already exist.

Prof. Constantin argued that we therefore need to re-think the notions of enterprise and social interest, by re-taking into account stakeholders. This had driven, among other things, the proposal to change Article [1833](#) of the Civil Code that was made when the report '[For a positive economy](#)' was published in the Documentation française in 2013: 'Any company must have a licit purpose, and be created and managed in the social interest. The pursuit of social interest requires the conciliation of economic, social and environmental dimensions, together with stakeholders'.

Thierry Philipponnat

In theory, investment is a practice for the long term. It reflects the long-term development prospects since a company grows over the years. However, in practice, a short-term orientation has predominated for the last 20-30 years. Now, we are beginning to see a shift back toward investment for the long term, which entails taking into account all environmental, social and governance (ESG) risks.

Investors generally take into account the criterion of governance, as the quality of governance is the basis of an arbitration quality/risk: when the quality of governance is not sufficient, this represents a significant risk for both the investor and the company.

Moreover, investors think of integrating ESG criteria to foster financial performance. Two studies, one by [Oxford University](#) and the other by [Columbia University](#), demonstrate a convergence between ESG performance and financial success.

However, active investors are a minority of global asset managers, and 20% of this awareness of ESG integration is concentrated in Paris. This trend has been reinforced in France by the adoption of non-financial reporting legal requirements (Article 225 of Law no. 210-788 of 12 July 2010 on national commitment to environment) and by COP21.

Mr. Philipponnat suggested that Environmental and Social criteria are only taken into account by investors in the event of crisis, while governance has a much stronger and lasting impact in the event of proven risk.

Plenary discussion

The discussion revolved around the notions of “Why?” and “How?”.

Today there are provisions for the consideration of ESG criteria, such as article 173 of the law of energy transition. However it was generally accepted that the “How?”, i.e. by which legal means, necessarily follows the “Why?” and implies a transdisciplinary approach.

Share issuers are asking to know the techniques to be used to define socially responsible investment investment (SRI). There is also the problem of comparability of different international corporate social responsibility (CSR) standards.

Moreover, governments tend to develop their CSR policies on the basis of consensus with industry stakeholders. CSR is presented as a way for business and society to address these environmental and social challenges. In order for companies to fully integrate ESG criteria, it might be wiser to go beyond this approach, which relies on the lowest common denominator, by presenting such integration as a way to to obtain financial outperformance and to guard against societal, environmental and reputational risks.

Results of the working groups

Board of Directors

The Board of Directors decides CEO compensation. The working group suggested that variable pay be linked to long-term criteria. The goals to be achieved in the long-term would be defined and a control lasting between 5 to 10 years would say whether the goal is reached. If so, the salary would be paid.

This could therefore happen retroactively, even if the CEO is no longer in office. In practice, this process requires that the Board define long-term financial and ESG criteria, and meet to determine whether the CEO has met her/his objectives. This raises the question of board composition, which should include stakeholder representatives.

Management

This proposal entails a proper revolution of corporate management and is based on the adoption of the law on duty of care and the [Sapin II Act](#) (France). Concretely, it is proposed to integrate stakeholders (employees, subcontractors, etc.) in the board with gender parity. In addition, four committees would be created: audit, compensation and appointment, risks and ethics, and strategy. The risks and ethics committee would be responsible for setting ESG criteria. A direct relationship is further established between investors and the audit committee, on one hand, and between the HR manager and the ethics committee, on the other hand. Finally, an office receiving all ESG-related alerts and information is created with a direct relation to the risks and ethics committee, so as to allow for better consideration and implementation of ESG criteria, as well as the measurement of such implementation. The potential opponents to this proposal are managers, administrators and investors who do not take into account ESG factors. To overcome these barriers, dialogue and use of media are useful, although natural pruning (i.e. retirement) should resolve part of the problem.

Employees

The working group proposed to allow employees to express themselves in the annual CSR report (which is part of the annual management report). In practical terms, employees could publish a statement and their position would be reflected in 1-2 pages of the management report. The Board could oppose such a proposal, having a dim view on that kind of information being expressly stated in the management report. To remedy this opposition, dialogue and coalition-building among NGOs and other SRI actors is necessary. There are also several institutional barriers. Mainly, whereas the state seeks to condense the annual management report, the current proposal would add pages. One solution is to publish the information digitally. Additionally, employees already have a legal right to express an opinion on executive pay but few are aware of this right, and it is even less frequently exercised ([article 2323-8](#) of the French Labour Code). Finally, the proposal echoes the stalled EU draft directive on banking reform (the so-called '[Barnier](#)' Directive (2016)) and would come together with the adoption of the French law on duty of care, or even together with a new definition of social interest (Article 1833 of the French Civil Code) that would take into account stakeholders' interests.

Investors (medium and long term - for whom ESG criteria are essential)

The objective of this working group was to discourage short-term investment and promote patient capital. They proposed to create a private mutuality, which would tax short-term investments to collect a fund to compensate the potential losses of mid and long term investors. This proposal reprises an existing practice: the issuance of premium Class A with special voting rights or other benefits to fund innovative projects (thereby promoting the interests of medium and long-term investors).

The final report of the global roundtable series will be presented in Brussels on September 28, 2016. More information is available on the Purpose of the Corporation Project [website](#).

The roundtable, co-organised by Frank Bold¹ and the SMART Project, University of Oslo Faculty of Law², brought together leading experts on governance from across Scandinavia to discuss corporate purpose and best practice how should corporate governance contribute to long-term sustainable value creation. The roundtable was part of a global series organised as part of the Purpose of the Corporation Project³ with previous events held in London, New York, Zurich, Breukelen (the Netherlands), and Paris. The keynote speech was delivered by Idar Kreutzer (Finance Norway). In addition, Markus Kallifatides (Stockholm School of Economics) presented research on the corporate governance practice of the Nordic region, while Prof. Beate Sjøfjell (University of Oslo) introduced recent corporate governance developments and updates in the European Union. The following roundtable discussion was held under Chatham House Rule.

Keynote Speech: Idar Kreutzer, Finance Norway

Mr. Kreutzer's speech focused on the role of the company in society. He started his presentation by quoting Aristotle: "Wealth is evidently not the good we are seeking; for it is merely useful and for the sake of something else".

Mr. Kreutzer then raised the question of whether the world is now facing a tipping point. In the last decades the world has become more integrated, with more global trade and strong international institutions. This is now changing: there is a lack of trust in transnational cooperation, with Brexit being one illustrative example. Is the trend in today's society, bringing politics that focus more on short-term self-interest, and in that case, what consequences will this have for the global business world?

Mr. Kreutzer went on to look at the role of companies in this changing world, reminding roundtable participants that the purpose of the cooperation is neither to provide humanitarian aid nor to act as an NGO. Their role is to create value, produce goods and services, create jobs, develop skills and generate revenue for society – directly and indirectly. He advocated that one possible pitfall is to see companies as something fundamentally different to what they really are: a tool for balancing risk and creating the possibility of profit. This principle, however, does not mean that we should be indifferent to how companies generate their profits.

Mr. Kreutzer said he did not believe in overregulating companies and thereby restraining their possibility to serve as a value creator. He suggested that the solution is to balance stakeholder interests. This balance may be reached by working with the shareholder ownership community because shareowners design the governance structure of companies. Furthermore shareholders can help to establish investment principles that balance the social, environmental and profitable aspects of investing, thereby creating engagement and dialogue within companies. The role of investors should include engagement in standard setting, responsible engagement in governance of individual corporations, and risk management related to major social and environmental risks.

The key to this understanding is to share knowledge and experiences through communication within and between companies and investors. Developing shareholder (stewardship) strategies is a better way to reach our sustainability goals than through increasingly rigid regulations. But realistically, he stated, this strategy

is unfolding very slowly. On a positive note, he pointed to a growing movement in the investment community, represented by the UN-supported Principles for Responsible Investment.

Finally, Mr. Kreutzer shared his view on universal standards and principles, such as the UN Principles on Business and Human Rights.⁴ He argued that we must not underestimate the values of such principles as a means to reaching the goal of sustainability. Such universal principles serve a useful role as guidance and inspiration for companies when they create their own internal standards.

Corporate governance developments in the EU and remaining challenges

Prof. Beate Sjøfjell⁵ emphasized the significance of good corporate governance as crucial for the survival of the companies themselves, and for the contribution of business to ensuring the achievement of the UN Sustainable Development Goals. She argued that the regulatory framework should seek to ensure that companies create sustainable value while staying within the planetary boundaries. Good corporate governance should thus lead to corporate sustainability; to the creation of value that on aggregate contributes to economic, social and environmental sustainability.

Prof. Sjøfjell went on to highlight recent developments in the EU:

- The ongoing reform process of the Shareholder Rights Directive, currently blocked in trilogue negotiations between the European institutions.
- The tentative discussion of shareholder duties in the EU, inspired by the international trend of stewardship codes. This is not expected to move very far, given the strong shareholder focus that dominates the EU corporate governance framework.
- The Non-Financial Reporting Directive, which was adopted by the EU in 2014, is a positive step but it does not prescribe verification (assurance) of what is reported, which is important in order to provide reliable information to investors.

Prof. Sjøfjell ended by pointing out that the biggest remaining challenge for corporate sustainability is the social norm of shareholder primacy, which she suggested should be mitigated to allow corporations to contribute to the systemic change that is needed to confront societal challenges.

Markus Kallifatides, Stockholm School of Economics⁶

Dr. Kallifatides presented findings from a recent empirical study conducted on 36 mid-cap and large corporations in Nordic countries to determine how and what affects corporate governance practice in the Nordic region.

The researchers conducted interviews with controlling shareholders, chairs and CEOs of participating corporations, with the intention to unveil and understand which factors influence corporate governance practice. In the Nordic region, companies typically have a controlling shareholder. The study found the profile of this controlling shareholder is decisive in how corporate governance is applied and practiced. The share ownership structure (dispersed or concentrated), level of commitment, category (State or private), degree of autonomy, and legal form (corporation, association, foundation) of the controlling shareholder play a key role. Under Nordic company law, controlling shareholders are potentially very powerful in relation to executive management, but the law provides little guidance how shareholders should exercise that power..

The researchers found five dimensions of shareholding that influence corporate governance practice:

- Personality/Character (risk attitude, philosophy, private/state owned etc)

- Intention (benefiting a state, enriching an individual or a family, time horizon, etc)
- Wealth (capability of participating in issue of new shares)
- Competence (capacity to make judgement – operational or financial)
- Reputation

They also found that shareholders select board members whose attitudes to ROI, ideas and ideals match their shareholding profile. In corporations with a controlling shareholder, the ownership profile will therefore to a large extent determine business strategy.

Dr. Kallifatides went on to speak about how this research also showed that the company laws of the Nordic countries allow a substantial amount of “tailoring” of the corporate governance practice, as the regulations allow and reinforce the strong position of dominant shareholders.

Since codes of corporate governance apply on a comply-or-explain basis, and they lack effective sanctions, they tend to be superficially respected and easily circumvented. The reasons why corporations opt not to comply with code provisions vary: the code may be seen as impractical, unnecessary, or an administrative issue. Based on his research, Dr. Kallifatides is skeptical of the idea that corporate governance codes can effectively promote sustainable corporate governance.

Finally, Dr. Kallifatides commented on how the chair has a special standing on the board in Nordic countries. Although the regulation does not differentiate between the chair and other board members, in practice the chair tends to be a predominant figure.

Roundtable discussion

Prof. Jukka Mähönen⁷ moderated the round table session. The following questions framed the discussion at the Oslo roundtable

- How can sound corporate governance foster long-term focus and sustainable behavior?
- What incentives for short-termism exist in law and the Code of practice for Corporate Governance?
- How can board-level responsibility be promoted within Norwegian state owned enterprises?

In discussing these questions, the participants addressed several points. Key conclusions of this discussion included:

- The current corporate governance framework gives ultimate power to shareholders; it is therefore crucial that they embrace the long-term view. This remains a challenge.
- While it is not desirable to overregulate corporate governance, for certain sustainability issues it is necessary to change existing legislation.
- Compliance mechanisms can help companies to avoid legal risks and unethical behaviour. To be effective, such mechanisms must be transparent, i.e. disclosed, ideally verified, and implemented at all levels of management.
- For non-financial issues that are not regulated, it is important to further develop international standards and translate them into benchmarks in order to allow effective investor engagement.
- Corporate disclosure should include a clear statement of goals, steps taken to achieve these goals, and results. Corporate reporting should develop towards an integrated model.
- Incentives for directors play an important role in driving short-termism.
- The role of analysts is often overlooked; they should more carefully consider ESG issues and risks.

The role of corporate governance and of the regulation

The participants first discussed the role of the board. Some agreed that the decisive role of the board in corporate governance is an illusion. With 5-8 meetings per year, it is impossible to have the complete picture of the development of the company and of its operating environment. Furthermore, the information provided to the board members is often carefully selected by the CEO. Boards should not micromanage the business but rather focus on the overall strategy, culture, and disciplinary measures.

One participant stated that there is no conflict between maximizing profits, good corporate governance and sustainable behaviour – as one is impossible without the other, which should be documented by further research. However it was pointed out that tax-evasion and corruption can be extremely profitable and easy to hide.

The participants discussed the role of regulation in addressing this problem. Some agreed that it would be important not to over regulate corporate governance, but rather develop international standards which become the benchmark for sustainable businesses. But it was also pointed out that CEOs and board members often speak in favour of regulation in the areas of corporate non-financial performance and corporate governance. The reason for this is that it is difficult to defend business strategies and choices that favour sustainability over short-term profit if they go beyond legal requirements.

One participant pointed out that whilst investors agree on corporate social responsibility standards, they do not reflect them in their practice. Therefore in order to drive change, a change of legislation is necessary. On the other hand, if new legislation is passed in response to an immediate crisis, there is a high risk that the quality of such legislation will be low.

The role of compliance systems

It was pointed out that non-financial reporting is extremely important for investors who want to “make the right choices”. Investors need to look at how a company carries out its business (compliance with laws, ethics and non-financial governance standards), rather than focusing exclusively on what it delivers in terms of immediate financial returns. Investors need to read this information and assess it as they would financial information. In this respect, the challenge for investors and other stakeholders is to determine what an effective compliance programme should look like. Greater clarity is necessary in order to improve shareholder and stakeholder engagement.

The participants also discussed the link between corporate governance, due diligence and compliance mechanisms, and criminal law. Currently, companies can expect lighter sentencing in criminal cases if they can prove they have an effective compliance programme. This can work as an incentive, but may also represent a problem. When board members and owners are charged under criminal law, the tendency is to point to the corporation’s compliance systems (“compliance based defense”). To prevent using a compliance system as a mere façade, it should be implemented at all levels of the organisation and externally verified. However, irrespective of the quality of such systems, the corporate practice depends also on the risk the corporation accepts when entering into a new market or developing a new strategy, which should be also reflected in attributing criminal responsibility.

In this respect, one participant brought up the lack of enforcement of the anticorruption legislation in the Nordic companies as compared to the practice in the US. Strong enforcement would drive improvement of corporate compliance and governance in this area.

The role of corporate disclosure and of international standards

Several participants endorsed the view that shareholders and investors are key in driving change. They argued that international standards need to be developed in greater detail with respect to key sustainability issues so they can be employed as a benchmark in order to assist investors in their investment decisions and to create a level playing field for companies. In this respect, corporate disclosure – or “non-financial” reporting – is extremely important.

Idar Kreutzer pointed out that corporate governance is not a linear process, but a complex network of interactions that boards must understand. He suggested a simple three-step model for corporate disclosure to be implemented by boards that would help to foster a sustainable business and improve communication with investors:

1. State clearly your plans. In this respect, less is more: it is better to focus on one key area – preferably selected on the basis of international standards – rather than trying to get better at «everything» at once.
2. Implement change and document the steps taken.
3. Report on the consequences of what you have done. Even if the corporation achieved nothing substantial, it should be reported. This will be useful to avoid mistakes the next time the corporation considers making similar changes.

This will then provide a tool for implementation of sound corporate governance and it will provide useful information to investors and the financial community.

One participant suggested that non-financial reporting should be integrated with financial and strategy reporting and that these reports be verified by an independent body.

Drivers of short-termism

The participants noted that the drive for short-termism comes primarily from shareholders. The prevalent strategy of investors is to maximise returns in the shortest possible time by investing in companies that can provide them with the best and quickest returns. In the current corporate governance framework that gives ultimate power to shareholders. It is therefore key that they embrace the long-term view. If the government expects investors to act as responsible, long-term oriented shareholders, it must prove it is possible by acting in such a way in its own role as a shareholder.

The participants also discussed the role of directors in short-termism. They pointed to incentive systems that align directors’ personal interests with short-term results. In the Nordic countries, the culture is focused on building consensus. That means that if the prevalent norm is to focus on maximising short-term profits, it is difficult for any director to stand out and challenge this logic.

Finally, the participants pointed to the role of analysts whose practice has been focused on analysing financial reports and largely ignoring non-financial data, except in cases where the analysed corporation has already faced ethical or similar problems.

References

1. Frank Bold is a purpose driven law firm with four offices in the Czech Republic as well as offices in Brussels, Belgium and Krakow, Poland. The firm uses both business and non-profit approaches to solve social and environmental problems. Frank Bold provides legal expertise in corporate accountability and corporate

governance to the European institutions as well as to civil society, municipalities, and businesses. Frank Bold initiated the Purpose of the Corporation Project.

2. The SMART Project is an international research project with 25 partner institutions, coordinated by the University of Oslo Faculty of Law, and funded under the European Union's framework programme Horizon 2020, Grant agreement 693642. Project website: uio.no/smart.
3. The Purpose of the Corporation Project is a collaborative, independent initiative led by the purpose-driven law firm of Frank Bold (www.purposeofcorporation.org). The academic basis for the project is provided by Dr. Jeroen Veldman and Prof. Hugh Willmott, who run the Modern Corporation Project at Cass Business School, London (thomoderncorporation.org). Jeroen Veldman is Senior Research Fellow at Cass Business School, City University, London. He has held appointments at Cardiff Business School, the Utrecht School of Governance, Utrecht University and a visiting professorship at UPMF, Grenoble. His research addresses the historical development of the public limited liability corporate form and its status in and between organization studies, management, company law, economics, finance, accounting, politics, and corporate governance. Hugh Willmott is Professor of Management at Cass Business School, City University, London and Research Professor in Organization Studies, Cardiff Business School, UK. He has held visiting professors at Copenhagen Business School and the Universities of Uppsala, Lund, Innsbruck, Sydney and the University of Technology, Sydney. He previously held professorial appointments at the UMIST (now Manchester Business School) and Cambridge. He co-founded the International Labour Process Conference and the International Critical Management Studies Conference.
4. UN Guiding Principles on Business and Human Rights http://www.ohchr.org/Documents/Publications/GuidingPrinciplesBusinessHR_EN.pdf
5. Professor of Law at the University of Oslo and coordinator of the SMART project.
6. Dr. Markus Kallifatides, Associate Professor at the Stockholm School of Economics and Director of the Center for Governance and Management Studies.
7. Dr. Jukka Mähönen, Professor at the University of Oslo, Faculty of Law.



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