

ecoDa

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Confédération Européenne des Associations d'Administrateurs
European Confederation of Directors' Associations

“CSR: What’s in for directors?”

an ecoDa paper

I- Definitions of CSR and CG are not distinct from each other

Past definitions of CSR and Corporate Governance

The most common definition of Corporate Social Responsibility states that *“CSR is about how companies manage the business processes to produce an overall positive impact on society”*. Two elements are essential; the quality of the management and the nature of the impact on society in the various areas.

In 1992, according to the Cadbury Code, the definition of the Corporate Governance did not refer at that time to the interest’s stakeholders: *“Corporate governance is the system by which companies are directed and controlled. Boards of directors are responsible for the governance of their companies. The shareholders’ role in governance is to appoint the directors and the auditors and to satisfy themselves that an appropriate governance structure is in place. The responsibilities of the board include setting the company’s strategic aims, providing the leadership to put them into effect, supervising the management of the business and reporting to shareholders on their stewardship”*.

Since that time, the **two definitions have become increasingly overlapping**.

Recent definitions of CSR and CG

In April 1999, the definition of Corporate Governance given by the OECD introduced explicitly the notion of stakeholders: *“Corporate governance is the system by which business corporations are directed and controlled. The corporate governance structure specifies the distribution of rights and responsibilities among different participants in the corporation, such as, the board, managers, shareholders and other stakeholders, and spells out the rules and procedures for making decisions on corporate affairs. By doing this, it also provides the structure through which the company objectives are set, and the means of attaining those objectives and monitoring performance”*. Corporate social responsibility and social reporting have been defined as corporate governance in action.

In 2001, the EU Commission defined CSR by using the word “governance”: *“By stating their social responsibility and voluntarily taking on commitments which go beyond common regulatory and conventional requirements, which they would have to respect in any case, companies endeavor to raise the standards of social development, environmental protection and respect of fundamental rights and embrace an open governance, reconciling interests of*

*various stakeholders in an overall approach of quality and sustainability*¹.

Furthermore, even if there is no direct link between CG and CSR in any of the European countries, the most recent national codes of CG refer increasingly frequently to stakeholders' interests. That is the case of the Belgian, Luxembourg, Slovenian, Czech and Spanish codes (a quick overview of the European CG Codes shows that the Slovenian code goes further than the others by recognising transparency towards stakeholders). In addition to a revision of its current CG Code, the United Kingdom has just passed the 2006 Companies Act which requires directors to act in the interests of stakeholders.

Stakeholders' interests and Corporate Governance

International level	
OECD	The OECD principles expressly mention the role of stakeholders in Corporate Governance and state that <i>"the corporate governance framework should recognise the rights of stakeholders established by law or through mutual agreements and encourage active co-operation between corporations and stakeholders in creating wealth, jobs, and the sustainability of financially sound enterprises"</i> .
ICGN	A declaration of ICGN in 1999 states that <i>"Boards that strive for active cooperation between corporations and stakeholders will be most likely to create wealth, employment and sustainable economies. They should disclose their policies on issues involving stakeholders, for example workplace and environmental matters"</i> .
European countries	
Belgium	No specific mention of the interests of shareholders, however the Buysse code refers to the relations with banks, suppliers, clients, employees, public institutions and external consultants
Czech Republic	The Czech CG Code repeats the OECD principles: <i>The corporate governance framework must recognize the established rights of stakeholders and encourage active co-operation between corporations and stakeholders in creating wealth, jobs, and the sustainability of financially sound enterprises.</i>
Finland	No mention of the stakeholders' interests
France	No mention of the stakeholders' interests
Germany	No mention of the stakeholders' interests
Italy	No mention of the stakeholders' interests
Luxembourg	<i>"corporate governance is intended to encourage and enable the board and management to pursue objectives that are in the best interests of the company, its shareholders and other interested parties, such as the company's customers and personnel"</i> . (April 2006)
Slovenia	<i>"In relations with other stakeholders (employees, creditors, customers, suppliers, the natural and business environment and the state) a company should exercise its rights responsibly and fulfil undertaken obligations in the manner that is compatible with the company's goals and that serves its long-term interests.</i> 1.4.2. <i>For the duration of the relationship with representatives of individual shareholder groups, a company should provide for a correct communication and mutual observance of confidentiality and of codes of good practices.</i> <i>It is recommended that a company warns all stakeholders of the manners of exercising their right which could damage the company or other company's stakeholders.</i> 1.4.3. <i>When deciding on a matter, a company should study and consider legitimate interests of all stakeholders, in particular the employees. Decisions, which have a direct impact on a given stakeholder group, should be immediately notified to this group by the company, unless they are considered a business secret or inside</i>

¹ *Promoting a European Framework for CSR*, Green paper, 18.7.2001

	<i>Information</i> ".
Spain	The board of directors " <i>will ensure that the company abides by the laws and regulations in its relations with stakeholders; fulfils its obligations and contracts in good faith; respects the customs and good practices of the sectors and territories where it does business; and upholds any additional social responsibility principles it has subscribed to voluntarily</i> ".(January 2006)
United Kingdom	Published in November 2006, the 2006 Companies Act includes measures that give greater clarity on directors' duties, including making clear that they have to act in the interests of shareholders, but in doing so have to pay regard to the longer term, the interests of employees, suppliers, consumers and the environment.

A recent initiative report from the Committee on Employment and Social Affairs of the European Parliament states "that the CSR debate must not be separated from questions of corporate accountability, and that issues of the social and environmental impact of business, relations with stakeholders, the protection of minority shareholders' rights and the duties of company directors in this regard should be fully integrated in the Commission's Corporate Governance Action Plan"².

- ***As time goes by, it seems that the perception of CG is becoming less and less internal to the company and increasingly comprises elements of CSR.***

II- CG and CSR are based on common principles

- Both CSR and CG operate by essential democratic principles such as *accountability and transparency*.
- They are both part of *ethics*. By considering the overall impact of business CSR is in itself ethical. Elements of ethical individual behaviour can be found in the concept of independent directors.
- Both CSR and CG are spread by *exemplarity*.
- Both CSR and CG can add value and contribute to *organizational performance and effectiveness of companies*.
- Both CSR and CG are about more than a process to meet an immediate regulatory requirement or a voluntary approach. It's about the *long-term success and sustainability of the enterprise*.
- Both CSR and CG question the statement "business of business is business".

III- The increasing interest in CSR and CG creates more overlap between them

To implement CSR and CG, two different approaches were chosen; CSR was initially based on a voluntary approach when the board's actions are subject to laws, regulations and approval of the shareholders in general meeting. It is true that CG is ruled in Europe by codes and regulations based on a comply or explain approach (which differs from the USA) and that there is a trend to increase CSR-related regulation. Some legislation in the European countries requires listed companies to prepare a detailed and certified report on

² http://www.europarl.europa.eu/meetdocs/2004_2009/documents/pr/638/638043/638043en.pdf

CSR as part of the annual report, as in France, the UK and the Netherlands.

CSR is now on the agenda of the European institutions. The European Parliament is arguing for more initiatives on CG. Institutional investment communities are increasingly demanding extra-financial information. Rating agencies invite companies to make corporate social responsibility part of their strategy. As a key issue for the reputation of the company, corporate social responsibility is also important for shareholders.

Danone has even just created a Committee on CSR within its board.

IV- Should CSR be real part of CG?

CSR should not be legally integrated to Corporate Governance. A corporate culture is required first. Some companies which pay attention to CSR are using it only as a communication tool; CSR is even sometimes handled by communication departments. We are far from having an effective CSR approach in companies. Imposing rules before a corporate culture would be irrelevant. Furthermore, there is no need for integrating the two concepts, CSR and corporate governance respond to different requirements.

However, **there are different reasons to encourage directors to deal with CSR:**

- Learning to think systemically and appreciating the organisation-wide effects of decisions helps considerably in making ethical decisions. Ethical, social and environmental considerations have to be part of strategic decisions to invest or do business, and of a company's day-to-day management.
 - ***Since the board has to pay attention to ethics and since CSR provides the organisation-wide effects of decisions, the board has to deal with CSR.***
- Moreover as a duty of care, directors must pay close attention to the issues facing the company and apply reasonable diligence and prudence in all decision-making on behalf of the company.
 - ***CSR can help directors to comply with their duty of care.***
- Directors are responsible for identifying risks. The inability to appreciate fully the impact of social issues (corporate culture, management personalities, and executive compatibility) has led to the failure of most mergers (FT 9 Nov 06, p.15).
 - ***Taking corporate social responsibility into account enables the company to reduce risks.***

As a forum for constant questioning, the board is undoubtedly the right place to deal with CSR and ethics in general. **It is not certain that CSR requires a dedicated committee within the board.** If we want to change spirit and habits, CSR should be handled by all directors collectively and their decisions regarding CSR should be submitted to the General Meeting on a collegial basis. This should not deter boards from strengthening examination of CSR in the Audit Committee or in the Ethics Committee.

Recommendations:

- ***Directors' watch-words should be: Ethics, Corporate Governance and Corporate Social Responsibility. Those three concepts have real concrete meaning if they are considered together.***
- ***As a forum for constant questioning, the board should deal with CSR and directors should move from a short-term perspective to a long-term perspective.***
- ***Paying attention to CSR within a board is part of directors' duty of care and must result from a collective and permanent process, even if the role of the Audit Committee or of the Ethics Committee can be strengthened with regards to CSR.***
- ***As part of effective risk management system, CSR risks must be taken into account by directors.***
- ***At this stage, no European legislation should be taken to promote CSR in Corporate Governance; it should be left to the professional bodies to strengthen good practices that directors can apply to all their activities.***