

## **Stakeholder Relationships**

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It is a pleasure to be invited back to address the Asian Roundtable on Corporate Governance. I attended the first of the Roundtables in Seoul and talked about Directors' Responsibilities. I remember throwing away my speech the night before my talk because, after listening to the first day of lectures, I decided what was needed was not a masterclass on the law but a more practical talk about what directors, and particularly non-executive directors, are expected to contribute to the running of a successful business. So I spoke from my own experience as Company Secretary of ICI.

Since the beginning of last year I have been Director of the Institute of Business Ethics, a small but growing charity, which advises and encourages businesses on high standards of business conduct. Companies subscribe to the Institute because they are concerned about sustaining their reputations. They are concerned that business and business leaders are not regarded as trustworthy. Every month another survey is published showing either that consumers believe industry is socially irresponsible or employees feel their managers are poor ethical role models or the public do not believe what companies say about the environment or human rights.

Speaking today from my experience as Director of the Institute of Business Ethics, it is now clear that stakeholders properly demand high standards of ethical and social

responsibility from companies. A successful company is one that can operate in harmony with the needs and aspirations of its stakeholders.

When I was a member of the OECD Task Force on Corporate Governance, I know there was some anxiety about including a section in the Principles on Stakeholders. It was one of the more heated discussions and what emerged might be criticised as placing undue emphasis on the contribution of employees and not enough on the relationships with other stakeholders such as suppliers, customers and communities. However, the Principles rightly encourage active co-operation between corporations and stakeholders and, importantly, require companies to provide access to relevant information to stakeholders. There is an important statement in the commentary to the Principles to the effect that *“concern over corporate reputation and corporate performance often require the recognition of broader interests.”*

Companies recognise that a significant part of their market value lies in their intangible assets and reputation is a major ingredient of those intangible assets. Trust is fundamental to a company's reputation and is the basis for the relationships between the company and its stakeholders. As our Chief Rabbi, Professor Jonathan Sacks, wrote in a British newspaper last month, *“Firms survive in the long run only by creating relationships rooted in integrity and trust.”* Transparency or openness is one condition for building trust, and I shall talk about stakeholder dialogue and social reporting in a moment.

What I believe is most important is that companies develop effective strategies for building reputation and earning trust. A corporate responsibility strategy should be based on the firm's values which are shared with its stakeholders. What people are interested in is how

those that operate in a market economy run their business. Are they making a better or a worse world? The protesters at Seattle, Prague and Davos were questioning whether the values of those in charge of businesses have any relationship to the values of society. The concept that is gaining ground which enables a strategy for corporate responsibility to be developed is sustainability or sustainable development. This concept goes way beyond environmental management. It examines the drivers for the long-term sustainability of a business which include the company's values and ethical principles. Such strategies will only succeed if companies first understand the expectations of their stakeholders as to what constitutes responsible behaviour. Back in 1987, the Brundtland Commission reported *"human survival and well-being could depend on the success in elevating sustainable development to a global ethic."* I think they were right and that is why it is so important that companies commit to sustainable development. As Shell have said such a commitment is the key to long-term business success.

Leading companies are now engaging in stakeholder dialogue and social reporting. They regard dialogue as important for gaining information and insights into their business. Such dialogue, if done well, provides a major input to the strategy for sustainable development.

The oil companies are good examples. When BP began to experience negative media reporting and increasing public hostility, they realised they had been mismanaging their communications with stakeholders. As so often, people preferred to trust the NGOs - the pressure groups - rather than the company. BP then started to measure and report on their environmental performance, they began to discuss issues openly with different stakeholders including the communities they were operating in.

In 1994, Shell began its Transformation programme following the public hostility to its operations in Nigeria and to its plans to dispose of the Brent Spar oil installation in the Atlantic. One element of its Transformation involved a worldwide programme of stakeholder dialogue in 1996 to understand their expectations of Shell. This involved 7,500 members of the public in 10 countries and 1300 opinion leaders in 25 countries, and 600 employees in 55 countries. Stakeholder dialogue is not cheap and it is not easy.

But it is not just the oil companies who engage in intensive stakeholder dialogue. Other sectors with reputations to defend include the National Lottery. Camelot, a fairly young company, operates the lottery in the UK. It is a controversial institution raising important public concerns. In 1999 Camelot carried out a social and ethical audit involving 6,000 individuals representing stakeholder groups, including the public, employees, the community, retailers, suppliers and investors.

But dialogue requires listening. One sector that has not been so smart at talking to its stakeholders is the biotechnology industry. Monsanto believed its development of genetically modified seeds was a winner. It believed the commercial and environmental benefits were outstanding. It turned into a PR nightmare as Monsanto in their US Headquarters failed to understand how European consumers might react. They did not engage in a dialogue with their consumers - in a search for common ground and constructive answers. They engaged in a debate aimed at convincing, and not a genuine two-way dialogue - as their Chairman has admitted, they forgot to listen. Over the last year, Monsanto has started to dialogue with its stakeholders but some have not forgiven them.

So good communication with stakeholders is an essential ingredient for establishing effective relationships. You can never communicate too often. We all know that however many times we tell the story someone will not have heard it or will not have understood.

Stakeholder dialogue not only provides information that can be used by the company in developing effective strategies and performance benchmarks for sustainable development. It is also the basis for reporting and communicating the company's impact on society. A significant number of major companies in the UK and elsewhere are experimenting with social reporting. Again, this has to be done professionally and thoroughly if it is not to be dismissed as PR hype by a cynical public. A number of voluntary reporting standards are emerging, including the Global Reporting Initiative, and such standards will be needed eventually if stakeholders are to be able to compare one company's report with another.

The benefits of social reporting include:

- Such transparency helps to build trust and enhances reputation
- The measurement and verification inherent in such reporting, together with the feedback following the report, stimulates the company to learn and to improve its performance
- It demonstrates a serious intent with regard to social responsibility
- It shows the company's actions are true to its values
- It motivates staff for their involvement in, and support of, the company's social and environmental programmes

In the UK, the current Review of Company Law is proposing that all larger companies should be required to include in their Annual Report an Operating and Financial Review (OFR). The OFR would include matters such as:

- The company's purpose, strategy and drivers of performance

And to the extent they are considered by the directors to be 'material':

- An account of the key stakeholder relationships on which the company's success depends
- Corporate governance - values and structures
- Policies and performance on community, social, ethical and reputational issues
- Environmental policies and performance

The integration of reporting to cover not only financial but also social and environmental issues permits a 'triple bottom line' form of accounting or a development into 'sustainable reporting'.

The number of UK companies publishing social reports increased from three in 1996 to 28 in 1999 and about 70% of the 100 largest public companies in the UK published formal environmental reports.

Although stakeholder dialogue, as practised by leading companies, and social reporting may be innovations there is nothing new about companies investing in their relationships with those who have an interest in the operations and performance of the company.

Companies have long understood that they ignore the interests of their customers, their employees or the pressure groups at their peril.

Companies on the whole object to being held accountable to their stakeholders and the UK's Company Law review is not proposing to go down that route. Some critics suggest that the stakeholder theory is also incompatible with corporate governance because governance is all about accountability. They argue that the directors of a company can

only be accountable to the shareholders. But governance is also about increasing prosperity and about corporate success. In that sense good stakeholder relationships are essential, and companies are learning that whatever may be the intellectual arguments over accountability, in practice their 'licence to operate' depends on sustaining their reputations with their stakeholders as trustworthy businesses. Businesses know that such trust has to be earned through being transparent and through effective communications. At the end of the day, business will be judged on its performance not on the quality of its reporting, but the disciplines of dialogue, measurement, reporting and verification will reinforce the high performance culture that most companies are seeking.