



**CHARTERED SECRETARIES
AUSTRALIA**

Leaders in governance

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Dear John

Corporate social responsibility

Chartered Secretaries Australia (CSA) welcomes the opportunity to comment on the CAMAC discussion paper *Corporate Social Responsibility*.

CSA is the peak professional body delivering accredited education and the most practical and authoritative training and information on governance, as well as thought leadership in the field. We are an independent, widely-respected influencer of governance thinking and behaviour in Australia and an expert commentator on issues affecting governance and legislation. We represent over 8,500 governance professionals working in public and private companies, as well as in the public and not-for-profit sectors, who have a thorough working knowledge of the issues relating to corporate responsibility.

In preparing this submission, CSA has drawn on the expertise of the members of our two national policy committees.

Yours sincerely

Tim Sheehy
CHIEF EXECUTIVE

Chartered Secretaries Australia (CSA)

Submission to the
Corporations and Markets
Advisory Committee (CAMAC)
in relation to
the discussion paper
Corporate Social Responsibility

CAMAC discussion paper *Corporate Social Responsibility*

Section 1.5

- (a) How might corporate social responsibility (CSR) usefully be described for working purposes?

One of the challenges in commenting on CSR is the difficulty of developing commonly accepted terminology and definitions. Terms such as CSR, corporate responsibility, sustainable development, socially responsible investments and triple bottom line reporting have become synonymous in the minds of many corporate directors, managers, investors and academics.

Definitions

To clarify how the various terms interrelate, it is useful to look at the definitions of individual terms:

Corporate social responsibility (CSR)

Some companies use sustainability or corporate citizenship instead of CSR. Some argue that the 'social' in CSR detracts from the business-related responsible activity by focusing on its social impacts (typically in the community area) while not giving due regard to the importance of ensuring the company's operations are run ethically and responsibly.

Fundamentally, CSR is about relationships between the company and its stakeholders and building trust. CSR is about how companies manage the business processes to produce an overall positive impact on society.

As noted in an article by Ann Durie published in CSA's journal, *Keeping good companies*, 'The aim of sustainability reporting is to report on this relationship of trust in a way that is believable. The only way to make the reporting credible is to *be* credible... For an organisation, being credible is about first determining with whom it has an interdependent relationship. The corporation is primarily responsible to those within its direct sphere of influence. The recognition of a tangible interrelationship with contextual parameters enables some form of qualitative or quantitative measurement'.¹

While the wording varies from one definition to the next, the elements remain fairly constant. The elements involve determining those individuals or groups with whom an organisation has a relationship of interdependence, that is, stakeholders.

Stakeholders

A stakeholder is an individual or a group that can affect the organisation, or is affected by the organisation's activities at any time, either now or in the future. This definition can include employees, suppliers, local communities, single issue groups, government and the wider society, as well as shareholders. As noted in the *ICSA Corporate Social Responsibility Handbook*², 'A similar, but more explicit definition of a stakeholder came from a conference in London and was quoted in the media column of *The Financial Times* on 14 September 2004 as: "Anyone that can bugger up your business"'.¹

¹ Durie, A, 'The writing on the wall: the CSR imperative', *Keeping good companies*, Vol 56, No 7, August 2004, p 403

² Hoskins, T, *The ICSA Corporate Social Responsibility Handbook*, The Institute of Chartered Secretaries and Administrators, London, 2005, p 181



Ann Durie further comments that, 'In a study in 1998, Warticke and Wood defined the power bases from which stakeholders operate.³ Those holding voting rights have formal power and are the traditional stakeholders, such as shareholders and directors. The groups able to affect revenue flows, such as employees, suppliers, creditors and customers, wield economic power. Pressure groups, the community, activists and governments hold political power. The sustainability reporting tools in current use determine stakeholders to be any of those from within these groups.'⁴

Sustainable development

The generally accepted definition of this term is that used in the Brundtland Report in 1987: 'development that meets the needs of the present without compromising the ability of future generations to meet their own needs'.⁵ Four moral concepts underpin this definition: equity today; environmental justice; intergenerational equity; and stewardship.⁶

Socially responsible investment

Socially responsible investment (SRIs) is the integration of personal values and societal concerns with investment decisions. 'SRIs provide a link between those individuals or institutions that hold investment capital and corporations that report on their social and environmental performance. The link is provided in a way that brings the activities and results achieved by the corporation into line with the investment mandate.'⁷

Triple bottom line reporting

Triple bottom line reporting to stakeholders focuses on the economic, social and environmental aspects of corporate activities. Information on the approach and performance of companies in managing the environmental and social impact of their activities, as well as financial data, is released by a corporation, to obtain a holistic view of the state of affairs within the corporation. Financial data is one indicator of the success of performance, but may mask systemic risks. The triple combination of reporting the social and environmental outcomes, as well as the financial aspects of a corporation's activities, provides information on the expertise of management and the potential risks associated with the operations of the corporation.

These concepts are inextricably intertwined, yet separate and distinct from each other.⁸

- (b) Which combination or combination of approaches to responsible corporate behaviour is most appropriate?

CSA is firmly of the view that no one approach or combination of approaches can be mandated as the most appropriate. Indeed, CSA believes that it is useful for companies and their staff to have an understanding of diverse concepts such as CSR, sustainable development, triple bottom line reporting and socially responsible investment, as this will allow each company to

³ King, D, *Corporate Citizenship and Reputational Value: The Marketing of Corporate Citizenship*, The Hawke Institute, University of SA, 2000, p 39

⁴ Durie, A, 'The writing on the wall: the CSR imperative', *Keeping good companies*, Vol 56, No 7, August 2004, p 404

⁵ World Commission on Environment and Development, *Our Common Future*, Oxford University Press, Geneva, 1987

⁶ Durie, A, 'The writing on the wall: the CSR imperative', *Keeping good companies*, Vol 56, No 7, August 2004, p 402

⁷ Social Investment Forum, *2003 Report on Socially Responsible Investing Trends in the United States*, SIF Industry Research Program, December 2003, p i notes that in the USA in 2002, a particularly bad year for stock market investments, socially responsible investment funds had a net inflow of \$1.5 billion, compared to all other funds, which experienced a net outflow of \$10.5 billion

⁸ Durie, A, 'The writing on the wall: the CSR imperative', *Keeping good companies*, Vol 56, No 7, August 2004, p 403



devise a CSR strategy most appropriate to that organisation's capacity to effectively monitor, measure and report on its CSR performance and its relationships with its stakeholders.

- (c) What are the incentives or disincentives for a company to conduct its business in a socially responsible manner?

The values of CSR sit at the heart of good governance. The OECD, in its introduction to its report *Principles of Corporate Governance*⁹, states that, from a company's perspective, corporate governance is about:

Maximising value subject to meeting the corporation's financial and other legal and contractual obligations. This inclusive definition stresses the need for boards of directors to balance the interests of shareholders with those of other stakeholders – employees, customers, suppliers, investors, communities – in order to achieve long-term sustained value.

The benefit of this approach towards corporate governance is that it recognises the broad objective of maximising shareholder value, while acting fairly in the interests of other stakeholders with an interest in the company's affairs.

There are those of the view that the corporation is a profit-seeking machine with a ruthless disregard for long-term consequences. This view implies that social issues are peripheral to the challenges of corporate management. It claims that the sole legitimate purpose of business is to create shareholder value. Proponents of this view believe that any argument proposing that a company should mitigate its social impact is irrelevant. The belief that a corporation's sole reason for existence is to increase its wealth was strongly expounded in the 1970s and can be traced to Milton Friedman's argument that: 'There is one and only one social responsibility of business: to use its resources and engage in activities designed to increase its profits'.¹⁰

The view that has greater traction in the twenty-first century is that the relationship between business and society is an implicit social contract. Proponents of CSR note that social issues are not tangential to the business of business but fundamental to it. This perspective holds that corporate managers holding onto a one-dimensional view of the corporation will not survive, nor will the companies they manage. Indeed, a recent global survey of corporate executives revealed that, overwhelmingly, executives embrace the idea that the role of corporations in society goes beyond simply meeting obligations to shareholders.¹¹

Supporters of CSR note that those companies alert to the long-term impact of social issues and in a constant dialogue with their stakeholders have a competitive advantage. Shifts in social issues that ultimately feed into the fundamental drivers of corporate performance generate value-creation opportunities. 'Paradoxically, the language of shareholder value may, in this respect, hinder companies from maximising their shareholder value. Focusing on a 'business is business' approach can lead managers to emphasise short-term company performance, while neglecting longer-term opportunities and issues, including societal pressures, the trust of customers and investments in innovation and other growth prospects.'¹² For reasons of ethics and enlightened self-interest, companies need to tackle such issues, both with words and actions. There is, therefore, considerable incentive for a company to conduct its business in a socially responsible manner.

⁹ OECD, *Principles of Corporate Governance*, first published 1999; revised 2004, Paris, OECD

¹⁰ Friedman, M, *The New York Times*, 13 September, 1970

¹¹ *The McKinsey Global Survey of Business Executives: Business and Society*, December 2005: *The McKinsey Quarterly* conducted the survey in December 2005 and received responses from 4,238 executives, more than a quarter of them CEOs or other C-level executives, in 116 countries

¹² Davis, I, 'What is the business of business?', *The McKinsey Quarterly*, 2005, No 3



There are powerful social rewards and sanctions associated with responsible behaviour. Acting responsibly generates trust, loyalty and goodwill among customers and employees, not to mention business partners. Corporate irresponsibility, on the other hand, can result in disapproval and suspicion, public criticism, damage to customer loyalty, loss of brand equity and a tarnished corporate reputation. Responsible behaviour creates a sense of satisfaction and self-respect among employees, whereas irresponsible behaviour can result in feelings of embarrassment, guilt, shame, cynicism and poor morale and loss of commitment from employees.

Disincentives, therefore, can include loss of reputation, incapacity to attract and retain good staff, shocks to the share price for listed companies, boycotting of products and services by customers and penalties imposed by regulators.

- (d) Do different or additional implications arise depending on the nature or size of the enterprise, for instance, the sector or industry in which an organisation operates, or whether a company has international operations?

It is sometimes argued that CSR is difficult for small to medium-sized enterprises (SMEs). It needs to be clarified that a socially responsible approach to business is not difficult for SMEs with an interest in long-term sustainability; however, reporting such approaches can be problematic.

This is because it can be costly to capture and provide the relevant information to demonstrate a company's responsible approach towards its society and environment, especially if that company is not already capturing such information for its management purposes. SMEs are less able to apply dedicated resources to the reporting of any responsible approaches they may take than are large organisations.

Owner-managers are already participating in responsible approaches, although they may not describe them as being part of CSR. Public discussion of the concepts mentioned above (CSR, sustainable development, socially responsible investment and triple bottom line reporting), leading in turn to greater familiarity with such concepts, will be useful to assist owners, managers and employees in all sizes of enterprise to clarify what constitutes CSR. Such clarity will assist SMEs not only to make informed decisions as to which approaches they believe to be most appropriate to them, but also to communicate with stakeholders using a shared language.

The reporting of CSR by larger companies in Australia note that they are beginning to encourage SME suppliers, through their supply chain, to become more CSR-active. For example, ANZ notes in its *Corporate Responsibility Report 2005* that it has 'developed a Sustainable Procurement Policy to be introduced into new and existing supplier contracts in 2006. The policy will guide the selection and evaluation of suppliers on the basis of environmental and social indicators consistent with ANZ's Environment Charter, including labour, health and safety standards and environmental impact'.¹³ The challenge is to ensure that the practices suitable in larger companies can be modified to suit SMEs. The learning inherent in any such challenge provides the opportunity for SMEs to embed such practices within their culture. Mandating one particular approach will cancel any such learning opportunities, as companies will not be engaged to devise innovative approaches to ensure their long-term interests and generate competitive advantage.

¹³ Australia and New Zealand Banking Group, *ANZ Corporate Responsibility Report 2005*, p 7



The nature of CSR in an SME can be significantly different from CSR in a large company. For example, many multinational companies report against international reporting initiatives that were developed specifically for large organisations with a global footprint. A large organisation operating in multiple jurisdictions is concerned with the organisation's impact, both direct and indirect, on the economic resources of its stakeholders and on economic systems at the local, national, and global levels, including such matters as employee wages, financial arrangements with customers and suppliers, and taxes. Environmental impacts include the organisation's products and services; energy, material and water use; greenhouse gas and other emissions; effluents and waste generation; impacts on biodiversity; use of hazardous materials; recycling, pollution, waste reduction and other environmental programs; and the cost of non-compliance with environmental regulation. Social indicators concern an organisation's impacts on the social systems within which it operates, which can include labour practices (for example, diversity, employee health and safety), human rights (for example, child labour, compliance issues), and broader social issues affecting consumers, communities, and other stakeholders (for example bribery and corruption, community relations).

It has been noted that it is a challenge for SMEs to adapt and narrow the broad citizenship concepts implicit in the global reporting initiatives so that they have relevance for the CSR agenda of those enterprises with either a less significant global profile or none at all. SMEs think locally and act locally and will seek to develop and foster their own approaches to socially responsible performance.

The question of whether the particular sector or industry in which an organisation operates has implications for companies' CSR approaches goes to the heart of the need to maintain choice in socially responsible approaches. This is because different industry sectors face unique sustainability issues. For example, while the extractive industry is more likely to have a far greater impact on the environment than the financial services sector, the latter does have an environmental impact and must consider the sustainability issues it faces in that regard. Looking at what the extractive industry is doing on this front will not necessarily assist the financial services sector to devise CSR approaches suitable to it.

- (e) In practice,
- (i) to what extent is corporate decision making driven by stakeholder concerns?
 - (ii) how do companies differentiate between various categories of stakeholders?
 - (iii) in what ways do companies balance or prioritise competing stakeholder interests?
 - (iv) how do companies engage with stakeholders?

(i) To what extent is corporate decision making driven by stakeholder concerns?

CSA notes that companies, of their own initiative, already engage in activities that are driven by stakeholder concerns, without such initiatives having been mandated.

CSA also notes that there is an array of legislation and standards that currently exists regulating the centrality of stakeholder concerns in corporate decision making, as follows:

- Companies are subject to various state-based environmental legislation.
- A new section, s 299(1)(f), was introduced into the Corporations Law by the *Company Law Review Act 1998* (Cth), requiring companies to report on environmental performance.
- Companies are subject to legislation regulating relationships with employees and occupational health and safety (OH&S) standards, both at the state and federal levels.
- The objective of the *Trade Practices Act* is to enhance the welfare of Australians by promoting competition and fair trading and providing for consumer protection.



Consumers are protected under the *Trade Practices Act*. In addition, the tort of negligence enables an individual to sue a corporation for a civil wrong caused by the actions of the corporation.

- Companies are subject to financial services and taxation legislation at the federal and state levels.
- The Australian Stock Exchange Corporate Governance Council (ASXCGC) guidelines, released in 2003, recognise the legal and other obligations that listed companies have to non-shareholder stakeholders such as employees, clients/customers and the community as a whole. Recommendation 10.1 notes that companies should establish and disclose a code of conduct to guide compliance with legal and other obligations to legitimate stakeholders.
- The *Corporate Law Economic Reform Program (Audit Reform and Corporate Disclosure) Act 2004* (commonly known as CLERP 9) commenced on 1 July 2004. It contains 13 schedules containing amendments to the *Corporations Act* and the *ASIC Act*. The financial reporting schedule (Schedule 2) deals with CEO and CFO declaration, management discussion and analysis (MD&A) and the new Financial Reporting Panel. The MD&A requirement is set out in the new s 299A. This section requires a listed public company directors' report to include information that members would reasonably require to make an informed assessment of the company's operations, financial position, business strategies and prospects. Any such information can include details of the company's engagement with stakeholders.
- Numerous voluntary codes of practice exist. For example, the resources sector developed the Minerals Industry Code in 1996, and 43 companies are currently signatory to this voluntary environmental management code.¹⁴ Other examples include the AusBiotech and ASX Code of Best Practice for Reporting by Life Science Companies, the United Nations Global Compact, the Global Reporting Initiative (GRI), and Voluntary Principles on Security and Human Rights for the Extractive and Energy Sectors.

Beyond legislation and standards, members of CSA, in both listed and unlisted entities, can point to a range of existing CSR initiatives within their organisations. Based on information provided by the companies of some of our members, a few examples follow.

Listed companies

National Australia Bank (NAB)

The NAB participates in the Carbon Disclosure Project, a global assessment by 85 institutional investors on the extent to which the Financial Times (FT) 500 most valuable companies are taking carbon risk and climate change risk into consideration as part of their core business. A further initiative is becoming a signatory to the Statement for Financial Institutions (UNEP FI) in 2002. The UNEP FI is a collaboration between the United Nations and 240 financial institutions globally working together for improved outcomes through lending and investment. As a member of the UNEP FI/Global Reporting Initiative (GRI) working group, NAB is working to develop the environment indicators for the Environmental Finance Sector Supplement to the Global Reporting Initiative (GRI – see later in the submission). The supplement includes the development of key performance indicators for direct and indirect impacts, including lending and asset management. In 2004, NAB became a member of a global working group, which consists of seven international banks that are working together to develop the global best practice management toolkit for measuring and reporting direct impacts of finance institutions. This benchmark standard is called VfU.

¹⁴ Bubna-Litic, K, 'Mandatory corporate reporting: Does it really work?' *Keeping good companies*, Vol 56, No 10, November 2004, p 616



NAB Australian businesses have facilitated an External Stakeholder Forum. The External Stakeholder Forum has representatives from prominent environment, community service and consumer groups, and indigenous and rural communities and has influenced the establishment of programs and facilities that seek to address financial services for low or vulnerable income members of the community.

NAB also supports the Total Environment Centre Green Capital Programs in Australia. The program aims to stimulate debate and raise awareness in Australia between environmental groups, community groups and business on environmental consequences of business operations and legislation. The NAB also designed its new building, National @ Docklands, with sustainability as a key design theme.

Caltex Australia Limited

Caltex Australia Limited undertakes contributions and sponsorship programs as part of its partnership with the community. The program is operated at three distinct levels: corporate sponsorships, that is, support for projects in the areas of welfare, the arts and education; regional sponsorship, which takes place with organisations in communities near Caltex's major company facilities such as their two refineries; and local support with individual service station operators and distributors responsible for handling sponsorship in their immediate areas. Caltex will support environment research, including community education, air quality, community volunteers, conservation, marine ecology, wetlands and endangered species; public information and policy research, including engineering, economics, petroleum industry, social policy, business analysis and research; education in engineering, finance, management, information systems and science and activities supporting the development and employment of young people; health and safety preventative measures and research, including health promotion, safety projects and emergency services; community support, including family support, volunteering, job creation and equal employment opportunity; support of the performing arts; and charity aimed at building a better community, including education programs supporting self-help.

BHP Billiton

BHP Billiton undertakes a range of activities in relation to CSR issues throughout the world and reports comprehensively on these activities each year in accordance with the GRI. BHP Billiton's 2005 Sustainability Report is available on its website. It is recommended that representatives of the Committee visit the website and review this report to gain an appreciation of the importance which BHP Billiton places on CSR.

Unlisted companies

Zurich Financial Services Australia Limited runs Community Connections. The program supports and encourages employees to engage with the community through the donation of their time and money. It is undertaken in partnership with United Way, a national not-for-profit organisation that supports a number of community organisations that make a difference in the lives of those in need at a local level. The program supports and encourages employees to engage in the community by:

- taking a day's paid leave to volunteer at a community organisation of their own choosing
- participating in a team volunteering day
- donating money from their fortnightly pay, matched dollar for dollar by Zurich.

Zurich also recently launched a national Green Office initiative that encourages its offices to be more environmentally responsible. The program will initially focus on reducing the use of paper, energy and water, as well as introducing a comprehensive recycling system in a number of its offices.



Flinders Ports Pty Ltd sponsors the South Australian Maritime Museum, and funds the education program 'A Day at the Port' through the South Australia Investigator Science Centre. This program is targeted at primary school children and educates them about the workings of a port and the link with import and export trades. It also concentrates on local community programs, including the funding of travel for children in regional centres to attend events in the city of Adelaide.

(ii) How do companies differentiate between various categories of stakeholders?

In practice, stakeholders have different needs and expectations and need to be dealt with differently. Companies need to engage with their stakeholders on a stakeholder by stakeholder basis. How companies do this will differ from company to company, as is shown in the examples members can point to of companies with a range of existing CSR initiatives.

(iii) In what ways do companies balance or prioritise competing stakeholder interests?

Although some commentators perceive a tension between the interests of different stakeholders, resolving the balance or prioritisation of those competing interests is part of a company's engagement with its stakeholders. A company will seek to identify the range of stakeholders, identify and rank issues through discussion with stakeholders, and map strategy against the issues, ensuring that a meaningful dialogue is held about the range of risks and opportunities that exists. This needs to take place regularly to ensure account is taken of changes in attitudes, not only in the company but also among the stakeholders. Thus any balancing or prioritising of competing stakeholder interests can only be conducted by individual companies in relation to their particular stakeholders. There is no manual to follow and an approach that works for one company will not necessarily work for another.

It is at the point of insolvency that stakeholder interests truly diverge, and there are existing mechanisms in the *Corporations Act* to deal with this.

(iv) How do companies engage with stakeholders?

Companies must be free to choose the forum, style and method of engagement with their stakeholders that best suits the needs of both the company and the different categories of stakeholders.

For example, the ANZ board has established a Nominations, Governance and Corporate Responsibility Committee, responsible for reviewing ANZ's approach to, and strategies for, ensuring CSR is integrated into overall business performance. This is underpinned by various charters, codes of conduct and policies, and the establishment of a Corporate Responsibility Council composed of senior executives who work across the group and also within their businesses to encourage participation in the CSR agenda, to ensure an ongoing dialogue and, in some cases, multi-layered partnerships, with stakeholders.

The BHP Billiton board has established a Sustainability Committee which oversees BHP Billiton's health, safety and environment and sustainable development functions. Engagement with stakeholders occurs at all levels, from the chairman's liaison with shareholders and others, to the local community engagement programs at each of BHP Billiton's sites around the world.

- (f) In practice, to what extent do stakeholders consider a company's socially responsible performance when making assessments or decisions about a company?

CSA notes that this issue largely lies outside the expertise of its members, although CSA notes that the reputational risk inherent in not attending to stakeholder needs is a factor that cannot be disregarded by any company seeking long-term sustainability.



- (g) Are there any changes that could enhance triple bottom line, sustainability or like reporting, including:
- (i) increasing the level of clarity and comparability of these reports?
 - (ii) any suggested changes to external verification of those reports?
 - (iii) whether any aspect of this reporting should be mandated and, if so, for what companies and what respect(s)?
 - (iv) are there particular issues for small to medium enterprises?

Although a number of social, environmental and ethical accountability tools are available in the public domain, there is no definitive reporting methodology for CSR. Research conducted in 2005 by CSA of members in listed companies showed that 79 per cent of such members have external bodies and organisations assessing and rating their organisation's CSR or asking the organisations to report on their CSR activities. Those same members note that 68 per cent of these reporting mechanisms do not share similar methodologies and measurement processes. This is in line with the fact that the surveyed members work in a variety of industries, and the reporting mechanisms reflect the industry-specific parameters.

A report gains relevance if it enables comparison between historical data and the implementation of future strategies and, currently, companies report against the most appropriate index for their industry. Industry-specific parameters can be determined and reported. This provides a gauge for outsiders, and the corporation itself, to assess its quality in relation to others within the same industry sectors. Identifying shortcomings and consequently determining strategies and setting goals for overcoming these is a vital element of the reporting process.

This is to be commended as the most appropriate way forward, rather than seeking one form of mandated reporting. Mandating one form of reporting will not provide for ready comparison of like with like. The ability for companies to recognise the key drivers that are most important to them will depend on their stage of growth, their operations and the communities in which they operate.

For example, the GRI has often been held out as a good model for mandated reporting. The GRI is a multi-stakeholder process and independent institution whose mission is to develop and disseminate globally applicable Sustainability Reporting Guidelines. Nonetheless, its mission has not been achieved, as the guidelines suit certain industries better than others. Furthermore, it has been acknowledged, including by the GRI itself, that its guidelines are not suitable for SMEs, although the GRI is keen to address this.

CSA also believes that mandating reporting adds a significant layer of additional costs to the operations of small listed and unlisted entities. Given the lack of evidence that small listed and unlisted entities are necessarily having significant impacts on the environment or the community, CSA does not believe that such a regulatory cost is justified. CSA strongly supports the continuation of voluntary reporting, with education provided to SMEs to communicate the value-creating opportunities inherent in CSR activity.

For example, in the extractive industry, smaller companies are seeking to attract capital and be competitive. If they do not voluntarily report against CSR indices on environmental issues, their capacity to attract capital and remain competitive will be hindered.

Verification of a company's CSR report involves costs and resources. CSA acknowledges that independent assessments are useful, but notes that, while large listed entities can afford the costs of such independent assessment, SMEs cannot readily afford them. Mandating verification would add a level of regulatory cost that CSA does not believe is justified for SMEs.



CSA also notes that the International Organisation for Standardisation announced in July 2004 that it is developing an international standard for CSR, aimed at providing guidance on implementing a CSR system to address social and environmental issues. CSA considers that Australia should monitor global initiatives in the field of CSR monitoring, measurement and reporting rather than trying to introduce a mandatory system that may conflict with global trends. CSA is not convinced that there is any benefit to the Australian community in pre-empting the ongoing international debate in this area.

CSA's members have expressed interest in seeing Australia consider examples of CSR initiatives in other jurisdictions such as the UK, where, for example, the London Stock Exchange has developed the Corporate Responsibility Exchange (CRE), which is an online tool that acts as a platform for companies to publish non-financial information, and for fund managers and research agencies to access it. Over half of the FTSE100 companies now use the CRE and our members would welcome similar voluntary moves in Australia.

Section 2.7

- (a) Whether, and in what circumstances, companies feel constrained by their understanding of the current law of directors' duties in taking into account the interests of particular groups who may be affected, or broader community considerations, when making corporate decisions.

As it stands, the law generally links a company's interests to those of its shareholders, and only derivatively with those of the community, consumers, employees and other stakeholders. With the increasing privatisation of public services, the expanding power of multinational corporations and the perceived diminution in the role of governments in the economy, the community increasingly looks to corporations as the provider of public goods and services. In light of this sociological evolution, many have questioned whether the law and community expectations sufficiently coincide, given that the law does not directly link a company's interests with those of stakeholders other than shareholders.

(i) Are shareholder interests the same as the interests of the company?

The *Corporations Act* states, in s 181(1), that:

A director or other office of a corporation must exercise their powers and discharge their duties:

- (a) in good faith in the best interests of the corporation; and
- (b) for a proper purpose.

It is important to clarify that the legislation does *not* state that directors and other officers must exercise their powers and discharge their duties in the best interests of shareholders, although it appears that case law has tended to grant primacy to shareholders' interests. It is a common misapprehension to believe that the legislation foregrounds shareholders' best interests and rights. It does not. It foregrounds the best interests of the company, which *generally* coincide with the best interests of shareholders.

CSA is of the opinion that the current legal framework governing directors' duties *does* accommodate directors having regard for the interests of stakeholders other than shareholders, as they must exercise their powers in the best interests of the company.



As noted by Bruce Cowley, in relation to the issue raised by the James Hardie case as to whether directors could be personally liable for being too generous in compensating victims:

Ultimately, the question for directors and officers is whether they have carried out their duties as required by law. In theory, it is true that if directors and company officers are too generous with shareholder funds they can be personally liable. Their principal duties are to act with care and diligence and to exercise their powers in good faith in the best interests of the company and for a proper purpose. Excessive largesse in settling claims (of any kind) might be regarded as failing to act with care and diligence.

However, directors and officers can argue the business judgment rule in defence of claims that they have failed to exercise the requisite standards of care and diligence. Under this rule, directors and officers will be deemed to have acted with reasonable care if they have made a decision in good faith and for a proper purpose about a matter in which they have no personal interest, a reasonable level of knowledge and a rational belief that the decision is in the best interests of the company....One would think that showing generosity to personal injury claimants might also constitute a proper purpose and be in the best interests of the company, especially if it impacts on the corporate brand.¹⁵

The discussion paper asks whether, and in what circumstances, companies feel constrained by their understanding of the current law of directors' duties in relation to CSR. CSA believes that the law as it stands *accommodates* a regard for stakeholders other than shareholders, which in turn provides for directors and companies to reveal through their activities how capable they are of generating the value-creating opportunities as a result of engagement with stakeholders.

In Cowley's article cited above, he also noted that 'The position of company officers is not getting any easier and some of the more cutting-edge examples seem to be arising in relation to James Hardie and its associated entities. Without arguing for yet more law reform, it is clear that some of our recent corporate controversies have put existing laws under considerable duress.'¹⁶

CSA notes that, despite the duress our corporate laws have been under in relation to CSR, those laws did nonetheless withstand the pressure. One high-profile case study of a company's attempts to engage with its stakeholders, including its shareholders, should not form the basis of legislative reform. The presumption that companies feel constrained by their understanding of the current law of directors' duties in relation to CSR stems largely from the pressures experienced by James Hardie Industries. CSA questions this presumption.

CSA believes that education as to the scope and application of directors' duties under the *Corporations Act* rather than legislative clarification via amendment will alleviate concern that the current law may prevent companies from taking into account stakeholder interests.

¹⁵ Cowley, B, 'Can directors be personally liable for being too generous in compensating victims?', *Keeping good companies*, Vol 57, No 1, p 36

¹⁶ *ibid*, p 37



- (b) If so, is there any useful scope for clarifying the current law in this respect and does the current law give directors sufficient flexibility to balance long-term and short-term considerations in their decision making?

CSA does *not* believe that revisions are required to the legal framework, particularly to the *Corporations Act*, to enable or encourage incorporated entities or directors to have regard to the interests of stakeholders other than shareholders and the broader community.

CSA believes that the debate generated by both the CAMAC discussion paper and the Parliamentary Joint Committee on Corporations and Financial Services Inquiry into Corporate Responsibility is fundamental to clarifying the current law. It will allow both companies and their stakeholders to understand that companies are not prevented by the *Corporations Act* from taking into account the interests of stakeholders other than shareholders.

Indeed, CSA is firmly of the view that any legislative clarification of the current law would create the very problems such clarification could seek to ameliorate. If the law is changed, it may mean that directors become less accountable (they are stewards of other people's money and have fiduciary responsibilities to the company), because their duties becomes generalised. The dilution of accountability would make it harder for shareholders and regulators to hold directors responsible for their decisions.

Companies and stakeholders alike should be reminded that CSR can be tailored to suit the company's circumstances by providing for it in the company's constitution. A clause can be included in a company's constitution permitting directors to take account of the interests of stakeholders other than shareholders, for example, 'for any purpose that the board sees fit'. CAMAC may wish to explore the possibility of exploring the inclusion of such a provision as a replaceable rule in the *Corporations Act*. Shareholders would decide whether they wanted it, or a revised version of it, as an object in the constitution. This would involve shareholders in the debate on CSR and enhance community education on this subject. The involvement of shareholders in such discussions would also ensure that they are actively involved in the decision making as to the importance placed on long-term interests in the corporations they invest in.

- (c) Are any changes needed to give the current law regarding the right of shareholders to express their view by resolution at general meetings on matters of environmental or social concern?

Currently the law requires 100 members to place resolutions before shareholders at a general meeting. From experience there have been few such resolutions, although it is clear from recent experience that they are increasing in number.

However, it is important to note that many of these resolutions have been submitted by special interest groups with little relevance or interest to the bulk of shareholders, retail or institutional. We believe that the requirement that such resolutions should be submitted by at least 100 members should be retained without reduction, as this represents a fair measure of support that the matter deserves to be discussed at an AGM. We believe that any changes to this latter requirement could see a proliferation of minor, irrelevant, vested-interest issues being included on the agendas of general meetings. This would only serve to make AGMs larger and longer, and would not necessarily serve the interests of the majority of shareholders.



CSA is not of the view that environmental or social concerns are irrelevant. These are issues that may be raised, and frequently are raised during questions at general meetings. They may be the subject of a resolution if 100 members or members with at least five per cent of the votes believe the issues to be important. CSA is of the view that, if less than 100 shareholders find the issue requires a resolution at a general meeting, then it is not possible to claim that the issue has a fair measure of support.

CSA notes that the Corporations Amendment Bill 2006 may or may not amend this provision. At the time of writing, the Bill had not yet been released.

Section 3.4

Should the *Corporations Act* be revised to *clarify* the extent to which directors may take into account the interests of specific classes of stakeholders or the broader community when making corporate decisions, or revised to *require* directors to take such interests into account?

CSA believes that those companies that ignore the long-term impact of social and environmental issues and that refuse to participate in a dialogue with their stakeholders are putting their long-term futures at risk. Such behaviour does not necessarily fit the legal requirement for directors to exercise their power in the best interests of the company.

CSA also believes that performance pressures will encourage companies to have regard for the interests of stakeholders other than shareholders and that this does not need to be legislated. Indeed, if it were to be mandated, having regard for stakeholder interests other than shareholders would likely become a compliance-driven, box-ticking exercise, rather than an innovative, value-creating opportunity to improve performance.

As noted earlier, CSA believes that the law as it stands *accommodates* a regard for stakeholders other than shareholders, which in turn provides for directors and companies to reveal through their activities how capable they are of generating the value-creating opportunities as a result of engagement with stakeholders. Education, fuelled by the public discussion generated by both the PJC inquiry and the CAMAC paper, will help clarify the extent to which directors can take the interests of stakeholders other than shareholders into account.

The public discussion to date has revolved around whether a permissive clause (permitting directors to take account of the interests of stakeholders other than shareholders), or a positive clause (requiring directors to take account of the interests of stakeholders other than shareholders) is needed in the *Corporations Act*. CSA does not believe that either is required.

In particular, CSA is strongly opposed to the idea of a positive requirement for directors to take into account the interests of stakeholders other than shareholders. As noted in the report of the UK Hampel Committee on *Corporate Governance* in 1997, '...the directors are responsible *for relations with* the stakeholders; but they are accountable *to* the shareholders. This is not simply a technical point. From a practical point of view, to redefine the directors' responsibilities in terms of the stakeholders would mean identifying the various stakeholder groups; and deciding the nature and extent of the directors' responsibility to each. That result would be that the directors were not effectively accountable to anyone since there would be no clear yardstick for judging their performance. This is a recipe neither for good governance nor for corporate success.'¹⁷

¹⁷ American Law Institute, *Principle of Corporate Governance: Analysis and recommendations*, Vol 1, American Law Institute Publishers, 1994, p 46



Furthermore, CSA believes it would be fraught with danger for legislation to include a 'shopping list' of stakeholders by listing specific classes of stakeholders. Specific classes of stakeholders can change with time, according to the stage of growth and the industry sector applicable to a company. Legislation would not keep abreast of these changes that mark the organic life of a company.

As noted earlier, a clause can be included in a company's constitution permitting directors to take account of the interests of stakeholders other than shareholders, for example, 'for any purpose that the board sees fit'. CAMAC may wish to explore the possibility of exploring the inclusion of such a provision as a replaceable rule in the *Corporations Act*.

Section 4.8

- (a) Are any changes to current statutory requirements needed to ensure better disclosure of the environmental and social impact of corporate activities?

A new section, s 299(1)(f), was introduced into the Corporations Law by the *Company Law Review Act 1998* (Cth). The first year of reporting was the 1998/99 financial year. The number of companies reporting on their environmental performance where their performance is subject to environmental regulation is increasing.

The *Corporate Law Economic Reform Program (Audit Reform and Corporate Disclosure) Act 2004* (commonly known as CLERP 9) commenced on 1 July 2004. It contains 13 schedules containing amendments to the *Corporations Act* and the *ASIC Act*. The financial reporting schedule (Schedule 2) deals with CEO and CFO declaration, management discussion and analysis (MD&A) and the new Financial Reporting Panel. The MD&A requirement is set out in the new s 299A. This section ensures that a listed public company directors' report includes information that members would reasonably require to make an informed assessment of the company's operations, financial position, business strategies and prospects. This reporting requirement accommodates non-financial reporting, including disclosure of the environmental and social impact of corporate activities.

Under ASX Listing Rule 4.10, companies are required to provide a statement in their annual report disclosing the extent to which they have followed the best practice recommendations in the last financial reporting period, including Recommendation 10.1 noting that companies should establish and disclose a code of conduct to guide compliance with legal and other obligations to legitimate stakeholders.

CSA does not believe that any changes are needed to current statutory requirements to ensure better disclosure of the environmental and social impact of corporate activities.

- (b) Are any changes desirable to any other reporting requirements, such as the ASX Listing Rule requirements, the ASX Corporate Governance Council Principles or relevant accounting standards, to provide more relevant non-financial information to the market?

The ASX Corporate Governance Council has responded to Senator Ian Campbell's request that it consider the issue of non-financial reporting for listed companies. The Council has agreed that it has an educative role to play in enhancing understanding of non-financial/CSR reporting, what it may cover, what investors are seeking from such information and the benefits to companies of such reporting.



The Council's great strength is that, as it is composed of 21 industry groups, the process of arriving at the *Principles of Good Corporate Governance and Best Practice Recommendations* was consultative and consensus-based. Hence the Principles achieved 'ownership' by the parties affected by them when they were issued. The Principles are also supported by the Listing Rules.

Given this consultative and consensus-based approach, the Council can play an important role in educating the corporate community and assisting the public discussion of what form non-financial/CSR reporting might take. It would be premature to pre-empt the Council's final recommendations on this issue, when it has resolved to issue a discussion paper for consultation in 2006.

- (c) In relation to any proposed further reporting requirements, should desired information be in a narrative or quantitative form?

It would be premature to pre-empt a decision as to the form and style of any non-financial/CSR reporting at this time. CSA believes that the debate generated by the CAMAC discussion paper, the Parliamentary Joint Committee on Corporations and Financial Services Inquiry into Corporate Responsibility and the proposed ASX Corporate Governance Council discussion paper on non-financial/CSR reporting are fundamental to clarifying how CSR information might be reported, according to industry sector and size of company.

- (d) It is possible to specify criteria to assist in comparing narrative disclosures, including by valuing or quantifying intangibles?

It would be premature to pre-empt a decision as to the form and style of any non-financial/CSR reporting at this time. CSA believes that the debate generated by the CAMAC discussion paper, the Parliamentary Joint Committee on Corporations and Financial Services Inquiry into Corporate Responsibility and the proposed ASX Corporate Governance Council discussion paper on non-financial/CSR reporting are fundamental to clarifying how CSR information might be reported, according to industry sector and size of company.

- (e) Would an additional environmental or social 'impact' reporting obligation be appropriate and feasible and, if so, how might it be stated?

CSA firmly believes that mandating an additional environmental or social 'impact' reporting obligation would be counter productive. The content of any such report will differ across industries and companies. Mandating such a report leads to the very real possibility of 'greenwash' reporting and public relations spin, as companies tick boxes against obligatory content that may have no relevance to their activities.

Underpinning this is the even more serious possibility of the development of a negative culture in relation to non-financial/CSR reporting. If a company is obliged to report against content that has no meaning for it, the company will not value its reporting. A desired culture is one where the board of directors and the management team are making active decisions as to the company's activities in its sphere of commercial activity, with full consideration given to the environmental and social impacts of each decision. This process can then be reported. Asking companies to report against mandated content works against the development of such a culture.



Also, CSA has already noted that those companies alert to the long-term impact of social issues and in a constant dialogue with their stakeholders have a competitive advantage. Shifts in social issues that ultimately feed into the fundamental drivers of corporate performance generate value-creation opportunities. Retaining a competitive advantage is about managing exposures over the long term. If non-financial/CSR reporting becomes solely a compliance exercise, it removes the incentive for corporations to compete with one another and seek investment on the basis of being 'ahead of the game'.

Furthermore, there is the question of what 'useful' information should be made available to stakeholders. Given the diversity of stakeholders, it is not surprising that they often have different and conflicting opinions as to what information is relevant. Different audiences want different information for different purposes. If a mandated reporting obligation were to be introduced, the attendant preoccupation with legal compliance and the reliability of the information would not automatically translate into a focus on the usefulness or relevance of information.

Section 5.7

- (a) To what extent are voluntary initiatives leading to improvements in corporate social and environmental performance?

It is salutary to compare voluntary initiatives in CSR now with what was happening only 10 or 15 years ago. There has been a dramatic, positive shift in CSR reporting, which was not mandated or regulated. The important point in noting this voluntary shift to embracing CSR approaches and strategies (and the reporting of same) is that it was an organic, evolutionary process rather than an imposed one. As such, it generated experiential learning that embedded the value of CSR in the culture of those companies that underwent the process. The learning took place in confronting the challenges and problems that arose on the journey. The process was not viewed as an obligatory one with punitive strictures attached to not following a mandated structure.

It was a voluntary process because companies saw the value in embracing CSR approaches and strategies. Over time new issues that cannot be identified today will emerge and those companies with a culture of 'looking outside the square' and actively identifying risks will be best placed to engage with those issues. If companies are concentrating on reporting against a shopping list of issues, such a culture is unlikely to be fostered.

For example, in 2005 BHP Billiton spent one per cent of pre-taxation profit on community programs and its shareholders supported this expenditure. BHP Billiton embarked on a journey of embracing CSR voluntarily and understands that engagement with stakeholders and regard to the environmental and social impacts of its activities goes to the heart of its licence to operate. The competitive advantage for the long term has been demonstrated and now many companies in the extractive industry take into account the interests of stakeholders other than shareholders. As one company innovates in this regard, others follow. This is how a cultural shift takes place.

BHP Billiton has also adopted a Matched Giving Program, where contributions of time or money by employees to community and charitable organisations are matched by the company. As noted earlier, Zurich Financial Services Australia Limited runs Community Connections. The program supports and encourages employees to engage with the community through the donation of their time and money. CSA notes that the Federal Government has facilitated the donations by employees to charitable institutions by providing for an immediate tax deduction, rather than asking employees to wait to receive the deduction.



(b) What lessons might be derived from any experience with voluntary initiatives?

The main lesson that has been derived from experiences with voluntary initiatives is how they embed a culture of CSR in a company.

By making CSR part of the normal business process, through embedding it in business decision making, the performance measurement system, employee and management incentive programs and the business planning process, CSR has a long-term effect on the company's culture.

Those companies that have undertaken voluntary initiatives have engaged in a process that allows them to:

- understand the range of stakeholders (and their relative priority) and identify their key issues in terms of both risks and opportunities
- audit the range of activities that already exist within the business
- decide where the company wants to position the business in terms of its CSR approach compared to those of its competitors and peers
- involve management and employees, both at the centre and in the operational business units, to determine the focused range of activities to which the company should be committed
- develop a CSR management system so that CSR becomes integrated within the business rather than being an add-on, or standing to one side (for example, as a compliance issue dealt with by the compliance division).

Ongoing public debate and discussion and education as to the benefits being derived by those companies that have embraced a CSR approach will assist those companies not yet fully aligned with the issues.

