A Peninsula for Governance Professionals - Strategy Governance and Sustainability

CS A. Sekar, Practising Company Secretary, Mumbai
Mr. Ranjith Krishnan, Assistant Professor, Head - Academic Programme Unit (APU) and Industry Liaison Officer, National Institute of Securities Market

INTRODUCTION

Strategy (or Strategic Management) and Governance (or Corporate Governance) are in reality two sides of the same coin. This is particularly so in the case of business enterprises organised in the corporate form, with one of the most striking and distinguishing features being the separation of ownership from the management. Globalisation and Liberalisation requires proactive response to the rapidly changing environment and this response to the situation is driven by the strategic business managers. In medium-sized and large business enterprises, there are three distinct groups namely shareholders, Board of Directors and the Management. The complexities in relationships between these three groups increase with the growing volume and size of business and the gap between the shareholders and the management widens. This gap is filled by having in place a proper governance framework. Apart from the economics of the business operations in terms of profits and / or wealth maximisation, rapidly growing business dynamics have their implications for the environment and the society as well. Since business enterprises are very much a part of the environment and the society in which operate, they have a responsibility to address the concerns of both the environment and society in a balanced manner, apart from their obligations to other concerned groups in the business entity such as employees, suppliers, customers, bankers and the regulators as well apart from their shareholders. Thus, emerged the concept of "stakeholders" instead of just "shareholders" and from a long term point of view for any business enterprise – a third dimension in the form of sustainability. The varying stakeholder concerns have expanded the scope of governance which links the strategy with long term sustainability.

CONCEPTUAL FRAMEWORK

Strategic Management

Strategic Management refers to the process of formulating, implementing and evaluating cross-functional decisions that enable a business enterprise to achieve its goals and objectives and is also concerned with a set of managerial actions and decisions that drives the long run performance of a business enterprise.

The Strategic Management process comprises of the following components: -

Fig. 1 Components of Strategic Management
Source: Metric Stream GRC Summit 2014 – Middle East

It will have to be understood and appreciated that each of the four components of Strategic Management depicted in Fig. 1 is a continuing as well as ongoing process, which are mutually interconnected and not necessarily sequential.

Corporate Governance

Good corporate governance is essential to develop added value to the stakeholders and going forward in times to come, preserve value for all the stakeholders by ensuring transparency always keeping in focus strong and balanced economic development. The concept of Corporate Governance was coined by Robert Ian (Bob) Tricker (who introduced the words corporate governance for the first time in his book in 1984) and according to him, "Corporate Governance is concerned with the way corporate entities are governed, as distinct from the way business within those companies are managed. Corporate governance addresses the issues facing Board of Directors, such as the interaction with top management and relationships with the owners and others interested in the affairs of the company" .

The Institute of Company Secretaries of India (ICSI) has defined Corporate Governance as "the application of best management practices, compliance of law in true letter and spirit and adherence to ethical standards for effective management and distribution of wealth and discharge of social responsibility for sustainable development of all stakeholders."

The foregoing definitions highlight the following important aspects: -

a) Definition of structure
b) Relationship between various stakeholders
c) Application of best management practices
d) Laws, procedures, practices and rules
e) Compliance of law in true letter and spirit
f) Adherence to ethical standards
g) Discharge of social responsibility
h) Sustainable development of all stakeholders

The scope of Corporate Governance includes both social and institutional aspects as it encourages a trustworthy, moral, as well as ethical environment. In other words, the heart of corporate governance is signified by the acronym ADRIFTS and companies would do well not to go adrift from "ADRIFTS", when it comes to Governance. ADRIFTS when expanded signifies Accountability, Disclosure, Responsibility, Integrity, Fairness, Transparency and Succession (ADRIFTS)

Corporate Governance can be regarded as the weaving thread that runs through an enterprise for creating and developing a corporate culture that is built upon the foregoing seven pillars namely ADRIFTS, which in combination determine the effectiveness of Corporate Governance.

With this background of Corporate Governance, in the following paragraphs, an effort is made to understand the concept and meaning of "Sustainability".

SUSTAINABILITY

Sustainability can be perceived as the way an entity creates value for its shareholders by maximizing positive and minimizing negative effects of environmental, social or economic issues.

According to the UN World Commission on Environment and Development (WCED): "sustainable development is development that meets the needs of the present without compromising the ability of future generations to meet their own needs."

Thus, it can be seen that in the concept of Sustainability there is a presumption that resources are finite and they should be used conservatively, judiciously and wisely keeping in mind the long-term priorities of the stakeholders and the society at large, as also to minimise the negative consequences of the way in which the resources are used.

Sustainability is a holistic approach that considers ecological, social and economic dimensions, recognising that all must be considered together to find lasting prosperity.

Pillars of Sustainability

Sustainability can be best explained with three pillars also referred to as the “Triple Bottom Line” approach. The three bottom lines or pillars, are:

- Social Sustainability
- Environmental Sustainability
- Economic Sustainability

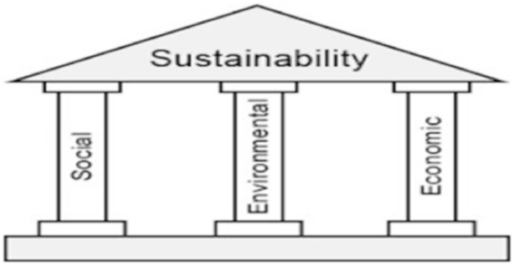

Fig. 2 – Three Pillars of Sustainability
Source: Open.edu

Corporate Sustainability

Thomas Dyllick and Kai Hockerts in “Beyond the Business Case for Corporate Sustainability” define Corporate Sustainability as, "meeting the needs of a firm's direct and indirect stakeholders (such as shareholders, employees, clients, pressure groups, communities, etc.) without compromising its ability to meet the needs of future stakeholders as well."

Corporate Sustainability can be best described as "encompassing strategies and practices that aim to meet the needs of the stakeholders today, while seeking to protect, support, and enhance the human and natural resources that will be needed in the future."

According to the Dow Jones Sustainability Index, ‘Corporate Sustainability is a business approach that creates long-term shareholder value by embracing opportunities and managing risks deriving from economic, environmental and social developments.”

Corporate Sustainability can be understood as the ability of companies to positively influence environmental, social and economic development through their governance practices and market presence. As a philosophy, it is a more viable alternative in the long run as compared to the traditional profit and wealth maximisation objective. Corporate Sustainability focusses on environmental protection and preservation as well as social justice and equity while at the same time recognising and balancing the apparent requirement of corporate growth and profitability. It is re-iterated, those enterprises that focus on sustainable growth and development would command greater respect, reputation and goodwill than those that focus only on shareholder gains and prosperity.

THE PENINSULAR CONNECT BETWEEN STRATEGY, GOVERNANCE AND SUSTAINABILITY

Strategic Management is connected with Corporate Governance in the sense that the definition of structure which is appropriate for the business enterprise and application of best management practices are of paramount importance requiring close involvement of strategic leaders, as the enterprise pursues its strategy while at the same time ensures that it is well governed.

Corporate Governance is connected with sustainability in the sense that the business enterprise discharges its social responsibility for sustainable development of all stakeholders and not just its shareholders or some selected group of stakeholders.

Arising out of the foregoing, it follows that Strategic Management processes have to connect and address the sustainability concerns to be effective and relevant not only in the immediate context, but in the long run for the future generations.

Strategic Leadership pursuing Corporate Sustainability seek to achieve long-term shareholder value by gearing their strategies and management to harness the market's potential for sustainability products and services while at the same time successfully optimising sustainability costs and risks.

Integrating Strategy with Sustainability through Sustainable Governance

A robust governance structure is a sine qua non for successful integration of a company's strategy with management of sustainability. The pre-requisite for such integration requires having in place committed leadership, clear direction and strategic influence coupled with strong, powerful and effective governance structures.

How and where sustainability fits into the overall corporate structure can be very revealing of a company's direction and priorities and in this context, it is important to appreciate that there is no cookie-cutter structure that can be applied; every company must tailor its approach for what makes most sense given its business model, structure, resources, and level of sustainability integration into the business.

It has been generally noticed that though enterprises are aware of the importance of the concept of sustainability to achieve corporate performance in the long run, sustainability is not integrated into the individual business processes particularly in the SME sector consequent to which while there is focus on the company's financial results, sustainability is not part of the Performance Measurement and Management systems of these entities. This is where Sustainable Governance systems come in handy through which sustainability is incorporated as part and parcel of the whole process of the strategic and operational management of the business. Strategic Management processes which incorporates the requisite sustainability parameters as part of the performance measurement and management systems coupled with Corporate Governance systems that addresses sustainability concerns on an ongoing basis leads to optimisation of the entire structure of the business in the long run.

Role of Governance Professional in this Peninsular Integration

Company Secretaries who are referred to as the Governance Professionals, either in their capacity as Whole Time Secretary or as Practising Company Secretaries (PCS) are the fulcrum in the process of this peninsular integration of Strategy, Governance and Sustainability. The role and the expertise of the Governance Professionals are displayed and highlighted in two distinct aspects – firstly in the development of the internal processes within the company for integration of strategic and operational processes followed with measurable, wherever possible and assessable sustainability outcomes and secondly in the reporting of the sustainability outcomes to the Board and onwards to the stakeholders as mandated by the regulatory framework.

It is necessary for the Governance Professional to impress upon the Board of Directors and the committees thereof that all Board and Committee members should have:

- generic sustainability skills and knowledge such as basic awareness of sustainability and how it affects the organization;
- basic understanding of what is corporate sustainability;
- ability to identify at a high level the most material sustainability impacts of and on the organization, its

value chain, industry and operating context;

- knowledge of key stakeholders and their priorities and issues;
- understanding of how poor sustainability performance can create reputational and other risks;
- ability to articulate how sustainability relates to the purpose and strategy of the organization;
- understanding of sustainability trends generally and as they affect the industry and their impact on the company; and
- knowledge of the company's business case for sustainability, including how sustainability can contribute to long-term value creation such as the ability to attract and retain talent and stimulate innovation.

Towards this end and also for the development of the internal processes within the company, the role of a governance professional could cover many aspects, some of which are as follows: -

1) Determine and implement amendments to governing documents, processes and structures to incorporate sustainability oversight roles for the Board and correspondingly ensure that managers, executives and key employees understand the emerging trends in corporate sustainability governance.
2) Ensure that the Board regularly reviews, updates and monitors compliance with corporate sustainability policies laid down by the company.
3) Include sufficient time for sustainability discussions in the agenda of the relevant committees and the Board of Directors.
4) Ensure that minutes of the meetings of the Board and the relevant committee documents the discussion on sustainability and other stakeholder related issues.
5) Development and communication of the strategy for sustainability initiatives and recommendations relating to them and link these initiatives and recommendations to the Board processes.
6) Initiate activities leading to increased stakeholder awareness about the benefits of a sustainable strategy.
7) Participate and co-ordinate the conduct of periodic assessments to identify potential short-term, medium-term and long-term trends and impact on the business arising out of various sustainability issues.
8) Participate in and co-ordinate the process of setting sustainability goals, targets and KPI's including development of the methodology to be followed for measurement of the actual performance on sustainability initiatives.
9) Ensure that there are systems for communication to the Risk Management Committee / Board about sustainability risks that impact the long-term competitiveness of the business.
10) Collaborate with the committees of the Board and the divisions / segments of the business on sustainability initiatives and risks.

In India, Securities and Exchange Board of India (SEBI) has prescribed the "Business Responsibility and Sustainability Reporting" (BRSR) which is mandatorily applicable to the Top 1000 Listed entities in India by Market Capitalisation. For other listed entities, BRSR is voluntary. The Company Secretaries as Governance Professionals have already been called up to play a major role in the implementation of the necessary procedures and systems for the integration of the sustainability practices and reporting under the new framework of "BRSR".

The BRSR format is divided into three sections namely:

Section A – General Disclosures

Under this section, the detailed disclosures are prescribed with respect to Details of the Listed Entity; its Products / Services; its operations; employees; Holding, Subsidiary and Associate Companies (including Jv's); CSR details and Transparency & Disclosure Compliances.

Section B - Management and Process Disclosures

In Section B, disclosures are mandated which aim at helping entities to demonstrate the structures, policies and processes that they have put in place towards adopting the NGRBC (National Guidelines on Responsible Business Conduct) Principles and Core Elements.

Section C – Principles wise Performance Disclosures

Section C requires disclosures aimed at helping entities to demonstrate their performance in integrating the Principles and Core Elements with key processes and decisions. Information is sought with respect to indicators that are categorized as "Essential" and "Leadership". It should be noted that disclosures with respect to essential indicators are mandatorily required to be disclosed by every entity to which the provisions of filing BRSR report is mandatorily applicable. Entities which aspire to progress to a higher level in their quest to be socially, environmentally and ethically responsible may voluntarily disclose information with respect to the leadership indicators.

The nine principles under which disclosures are sought distinctly under two heads (Essential Indicators and Leadership Indicators) are as under: -

Principle No.	Description
1	Businesses should conduct and govern themselves with integrity, and in a manner that is Ethical, Transparent and Accountable.
2	Businesses should provide goods and services in a manner that is sustainable and safe.
3	Businesses should promote the well-being of all employees, including those in their value chains.
4	Businesses should respect the interests of and be responsive to all its stakeholders.
5	Businesses should respect and promote human rights.
6	Businesses should respect and make efforts to protect and restore the environment.
7	Businesses when engaging in influencing public and regulatory policy, should do so in a manner that is responsible and transparent.
8	Businesses should promote inclusive growth and equitable development.
9	Businesses should engage with and provide value to their consumers in a responsible manner.

A CS (both in employment and in practice) are naturally "the preferred professionals" for advising and ensuring the compliances with respect to BRSR considering their exposure to Governance and Compliance Management systems in the corporate world, which will give them a definite edge over other professionals.

Pillars of the CS / Governance profession

The governance professionals / CS armed with the three pillars unique to Indian governance professionals namely Secretarial Standards, Secretarial Audit and the Auditing Standards issued by the ICSI (CSAS 1 to CSAS 4). In this sense, the Indian governance professionals have set a benchmark for the world to follow and adapt. The quest for integrating strategies into sustainability gets strengthened through the Secretarial Standards which streamlines the Board process. Adherence to the secretarial standards is in the exclusive domain of the whole-time company secretary.

Secretarial Audit by a PCS for listed entities and certain large companies based on thresholds is another unique pillar, which goes a long way in the form of an assurance function with respect to the corporate governance framework prevailing in the company that is being audited.

The third unique pillar is the Auditing Standards issued by ICSI (CSAS-1 to CSAS-4) applicable to a PCS accepting audit assignments (including secretarial audit).

While, as regards Secretarial Standards and Secretarial Audit, there is a need to dive deep with due care but with an open back of the mind that will lead the profession into the landscape where there is increasing focus on ESG and sustainability, the effectiveness of auditing standards is yet to be tested on the ground. However, there is no doubt that with the right approach and an open mind, these three unique pillars of the Indian Corporate governance system properly shaped towards a world- class framework should take us forward with confidence as we travel the path towards corporate sustainability in the true sense.

• • •