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Contents

Proposed CSR rules too strong for business, too weak for civil society......p.1
Commission accuses companies of 'group think', demands social responsibility......p.2
Sustainability leader urges firms to integrate CSR reporting......p.4
Sustainability chair: Going beyond the Commission's CSR proposals......p.5
Doubts surround corporate ethics on new 'comply or explain' regime.....p.7
UK threatens firms with gender quotas as women's appointments fall...p.8

Proposed CSR rules too strong for business, too weak for civil society

Proposals for disclosure of non-financial information by large companies to beef up corporate social responsibility (CSR) launched by the Commission yesterday (16 April) go too far for business interests, but not far enough for NGOs.

Launched in Strasbourg by Michel Barnier, the internal market commissioner, the CSR proposals would amend three accounting directives that require larger companies to report non-financial information, such as their diversity and environmental policies and to explain why they have not done so where necessary.

As a first step, EU member states have been given the possibility to apply the new rules to listed companies only.

Companies failing to do so would be required to explain why they have not included such information, in the first attempt to legally impose such a "comply or explain" regime on larger companies.

The proposals will need the approval of the European Parliament and EU states before becoming law.

Information is not needed for investors, say business leaders

BusinessEurope, a federation that represents Europe's largest companies, said in a statement that it was "disappointed" by the European Commission's decision, claiming that the obligations ran the risk of "demotivating all companies that have embarked on genuine CSR activities on their own."

"This proposal will create red tape and further disadvantage for a large number of European businesses in international markets, running counter to the urgent necessity of re-establishing the conditions for confidence and competitiveness in Europe," said Jürgen Thumann, BusinessEurope's president.

He underlined as a key concern business fears that disclosures in

Continued on Page 2

Continued from Page 1

corporate annual reports should be aimed squarely at the needs of investors, not other requirements, which are aimed at placating public policy aims, rather than the genuine needs of investors.

"If required solely for public policy reasons, [the information] should be kept out of the annual report," Thumann said.

Fewer than 10% of companies disclosing proper CSR information

His remarks were echoed by Nigel Sleigh-Johnson, the head of financial reporting at the Institute of Chartered Accountants in England and Wales (ICAEW).

Despite broadly welcoming the proposals, Sleigh-Johnson warned: "If the information is not bespoke and of relevance to investors, it will just lead to clutter and 'boilerplate'."

But the Association of Chartered Certified Accountants (ACCA) disagreed.

The global auditing body said in a statement that fewer than 10% of the largest EU companies currently disclose such information either regularly or properly.

"This approach will build trust with stakeholders, attract investors and help with the transition to operating in a green economy," said Rachel Jackson, head of sustainability at ACCA.

NGOs claim proposals too weak

NGOs welcomed the proposals, but criticised their lack of teeth.

"The private sector has a critical role in the fight against corruption in the EU, and these proposals will help determine if the biggest companies are playing their part," said Jana Mittermaier, the director of the Transparency International EU office.

She said that few companies currently indicate whether they prohibit "facilitation payments" – bribes paid to officials to speed up routine such as customs procedures – and reporting on the monitoring of anti-corruption programmes tends to be weak.

Meanwhile the European Coalition for Corporate Justice (ECCJ), an NGO, welcomed the proposal but stressed that "the current wording leaves companies too much flexibility."

"We fear companies will only identify and disclose the risks that affect their economic performance, and won't take responsibility for the impacts they have on the people and the planet," said, Jérôme Chaplier, the ECCJ coordinator.

Commission accuses companies of 'group think', demands social responsibility

The EU executive is due today (16 April) to accuse corporate Europe of lacking innovation and diversity as a result of "group think", as it unveils new proposals requiring larger companies to disclose information on a range of environmental and social impacts.

The proposals – to be launched in Strasbourg by Michel Barnier, the internal market commissioner – will echo global efforts to introduce new corporate social responsibility reporting obligations through a United Nations initiative.

Barnier's CSR plan, according an 11 April draft seen by EurActiv, proposes amending three accounting directives to require larger companies to report on non-financial areas, such as their diversity and environmental policies and to explain why they have not done so where necessary.

"Company boards with members who have a similar educational or professional background, geographical diversity, age or gender, may be dominated by a narrow 'group think'," the document says.

Lack of diversity hampers innovation

The EU executive claims that such attitude lessens challenges for management decisions, and "can also lead to a harder acceptance of innovative ideas accepted by management."

The degree of flexibility and enforceability will be fiercely argued. The draft proposes that smaller companies should be required to comply with fewer bureaucratic reporting requirements. For larger companies, however, the proposal would represent the first introduction of "comply or explain" reporting requirements for non-financial information.

"I hope that we will see some progress on measures to increase information to consumers and investors whilst at the same time keeping CSR firmly in the hands of businesses and with as little red tape as possible, especially for SMEs," said Swedish MEP Cecilia Wikström (Alliance of Liberals and Democrats for Europe).

The European Commission has had a difficult experience with CSR, but is hoping to put the matter back on the agenda.

The EU executive's moves echo international attempts to develop similar obligations.

Continued on Page 3

Continued from Page 2

A high-level UN panel is considering introducing CSR reporting in its successor to the Millennium Development Goals (MDGs), which expire in 2015.

Call for action at Rio

Calls for global CSR reporting standards were also raised at the UN's Conference on Sustainable Development last June in Rio de Janeiro, Brazil.

The Corporate Sustainability Reporting Coalition (CSRC), representing financial institutions, professional bodies, NGOs and investors, called at the Rio summit for the UN to commit to developing an international framework on non-financial reporting.

The Rio summit's final declaration included recognition of the importance of corporate sustainability reporting.

An official attending a 27 March meeting of the UN's high-level panel on the Post-2015 Development Agenda in Indonesia told EurActiv on condition of anonymity that CSR reporting was discussed with a view to keeping the issue on the UN agenda for inclusion in the post-2015 discussions.

The proposal under consideration is to develop a CSR convention comprising a commitment by UN member states to develop regulations, codes or listing within the annual report of all listed and large private companies.

Companies electing not to prepare such a report would be permitted to opt out but would be required to explain why they had done so to shareholders, creditors and other stakeholders.

Sustainability leader urges firms to integrate CSR reporting

European computer emergency response teams, which are being beefed up as part of the EU's cybersecurity strategy, need to set more 'honeypot' traps to snare cyber attackers, according to reports.

The Commission's proposals to introduce new corporate social responsibility (CSR) rules must push companies to incorporate non-financial reporting into their accounts, according to a campaigning executive.

The Commission's proposed new CSR regime, launched on 16 April, would require larger companies to report non-financial information, such as their diversity and environmental policies and to explain why they have not done so where necessary.

Steve Waygood, the head of sustainable and responsible investment with Aviva Investors, told EurActiv that he was generally "very pleased" with the proposal, but added: "It is not perfect and would have been better if it had introduced the concept of integrated reporting."

Integrate reporting into all parts of accounts

"Integrated reporting" would mean applying the non-financial standards to each separate part of the company accounts, rather than writing one CSR–style report and including this as an annex to the accounts, as the Commission's proposal suggests.

According to Waygood, the CSR data could impact on separate parts of the company accounts that way.

"What if sustainability issues matter to their business, or affect their resources, their employee base? I do not think they will be fully capturing this and implementing it if these things are simply put in an annex to the accounts, they should be across the whole accounts," Waygood said.

He emphasised how the remuneration report of a company could be affected.

"For example, if health and safety issues were a concern with the firm – for example it might be a mining company – then fatalities or lost-time injury rates could be reflected in the [directors'] financial remuneration," said Waygood.

A first step

According to the Commission, fewer than 10% of the largest EU companies regularly produce sustainability reports.

Around 18,000 companies will be affected by the new rules, compared to the 2,500 organisations that now disclose environmental and social information.

Two of the most commonly used reporting instruments are the United Nations Global Compact and the Global Reporting Initiative (GRI). For the Commission, enterprises using internationally recognised CSR guidelines and principles are likely to gain in credibility, but three in five companies still do not refer to these instruments.

GRI Deputy Chief Executive Teresa Fogelberg said the solution proposed by the Commission would provide a level playing field for those companies that are already reporting, but also encourage many more to embark on their sustainability reporting journey.

"In time, a tipping point would be reached, with a critical mass of companies playing their part in accelerating the transition to a sustainable global economy."

Make fund managers vote carefully

Waygood said that the Corporate Sustainability Reporting Coalition (CSRC) – a group of some 100 companies campaigning for CSR reporting – will not slow up as a result of the Commisssion's proposals.

"We are pushing for a [United Nations] sustainable development goal that says by 2020 every mid-cap company is publishing an integrated sustainability report," he said.

The best way to enforce such an obligation, Waygood believes, is to put the company's CSR report to the general vote of shareholders at the annual general meeting.

"There could be a standardised report that enables a client to see that fund managers meet certain requirements in their voting," Waygood suggested.

Sustainability chair: Going beyond the Commission's CSR proposals

Fund managers and other institutional investors should be scrutinised for their shareholder voting on social responsibility, says the founder of the Corporate Sustainability Reporting Coalition.

Steve Waygood heads insurance company Aviva Investors' sustainable and responsible investment and is the founder of the Corporate Sustainability Reporting Coalition. A former chairman and board member of the UK Sustainable Investment Forum, Waygood was part of the expert group that wrote the UN Principles for Responsible Investment and is a lecturer at Cambridge University's Programme for Sustainability Leadership. He spoke to EurActiv's Jeremy FlemingThe proposed legislation will oblige companies to be audited for preparedness and to notify national authorities of cyber incidents with a "significant impact."

What do you think of the Commission's proposed new CSR regime which would require larger companies to report nonfinancial information, such as their diversity and environmental policies and to explain why they have not done so where necessary?

The announcement has been a long time in the waiting and I am very pleased with it. I think the proposal would make a big difference. It is not perfect and would have been better if it had introduced the concept of integrated reporting.

What is integrated reporting?

The International Integrated Reporting Council is a special interest group consisting of industry players. I sit on the working group of the Council, and we believe that introducing sustainability issues throughout the entirety of corporate accounts would help to integrate sustainability into the DNA of the firm, because it would help to create conversations within internal audit, within risk functions, strategy and accounting. It could also impact on the remuneration report – where one exists – to determine how directors should be rewarded, along with other indicators such as customer satisfaction.

So you would like to see a more horizontal approach, with sustainability issues incorporated across all of the elements of the accounts?

The benefits we would expect to get would be more considerable, because we want to know that the cash flows for the company are sustainable for the future. Otherwise the company is only measuring these issues from a compliance perspective and not caring about what it means for their strategy, and how they need to change their business model, how they need to protect their reputation, report on their executives. What if sustainability issues matter to their business, or effects their resources, their employee base? I do not think they will be fully capturing this and implementing it if these things are simply put in an annex to the accounts, they should be across the whole accounts.

How could this work within the context of the remuneration report, by way of example?

There are hundreds of companies that already do this kind of CSR reporting on remuneration, and if you look at the remuneration report of any company, that gives you an immediate idea of the extent to which companies have these reporting mechanisms in place. The current [Commission] proposals talk about key performance indicators, but if they are genuinely 'key' they should be embedded into the remuneration report, not by means of a total effect on remuneration, but of a percentage, a modest but material percentage. For example if health and safety issues were a concern with the firm – for example it might be a mining company – then fatalities or lost time injury rates could be reflected in the financial remuneration. Other indicators such as employee engagement figures, customer feedback and regulatory compliance could also play a part.

You and Aviva have played a steering role in the Corporate Sustainability Reporting Coalition what are the aims of this consortium?

We are global investors, but based in the UK, so Europe is a key concern, but we are working through the UN to get a global solution to sustainability reporting. That is why we campaigned hard at the [United Nations's] Rio+20 summit to get commitments on that front.

Is there a danger that this will slow up now that the European Commission has announced its proposal?

Following the Rio+20 conference

Continued on Page 6

Continued from Page 5

we have added members, and now have around 100 members. The outcome of that Rio+20 summit document, at paragraph 47, says a lot and nothing. There is no new money, no new commitments or provisions for any difference, except to say that stakeholders should come together to correct this problem, so it recognises that there is a problem. So we were both pleased to have it in there at all, but deeply disappointed that it wasn't the effective treaty we were pushing for.

What can be hoped for now?

There are two things that have come out of Rio+20: the post 2015 process, and the sustainable development goals. The 2015 process is asking what will replace the UN's Millennium Development Goals, but sustainable goals are likely to replace them so these two issues are essentially the same discussion. We are pushing for a sustainable development goal that says by 2020 every mid-cap company is publishing an integrated sustainability report.

How could that be enforced?

Either by using ethical coercion or norms, as they are called, which would allow each country to apply pressure. We have no confidence that these types of voluntary mechanisms work, however. The second way is by legislating in company law, and that is what the EU is looking at in its ongoing re-assessment of corporate governance. A third way would be by integrating a "comply or explain" system into each stock exchange throughout the world, so that each company must comply or explain why not. We favour this and would we want that sustainability report published by each company at its annual general meeting, and voted on by investors, that is something that we do at Aviva.

How can you ensure that investors are more engaged when they vote, or indeed that they do vote?

We have recently given evidence on short-termism in corporate strategy for the UK's review by Oxford University's Professor Kay into the lack of stewardship of investors. The key issue is that he is focusing on the supply of stewardship, saying investors should take control, and he has proposed amongst other things an investor forum where they could pool influence at lower costs. Personally, I am less convinced that is true. I think the demand side was missed and I think we need is an informed demand from the customers of fund managers who should be exercising stewardship to supply that stewardship. That means demand from trustees, from foundations, demand from insurance companies, to ensure that the fund managers that they employ vote at AGMs and that they oversee and assess that voting and they see reports on that. There could be a standardised report that enable a client to see that fund managers meet certain requirements in their voting.

What do you think of the "Comply or Explain" system proposed by the Commission in its reporting proposals?

It is not clear what this will look like because for the penalties, the member states are going to be required to "discourage" companies that fail to comply, but it is not clear what that means.

In the UK it potentially involves losing your listing on the stock exchange and when that is dangled companies deal with the problem. No company has lost its listing but the threat of that sanction has generated good new disclosure. It has also generated noise and some bad disclosure. Which is why we suggest the reports should be put before a vote of the shareholders. Clearly not all votes are taken seriously but I think there are enough investors who do care that means that companies will have to take this seriously.

Doubts surround corporate ethics on new ‘comply or explain’ regime

Those for and against proposals launched this week to tighten corporate social responsibility reporting (CSR) are both suspicious of its “comply or explain” enforcement regime.

The proposed new CSR regime would amend three accounting directives that require larger companies to report nonfinancial information, such as their diversity and environmental policies and to explain why they have not done so where necessary.

Companies failing to do so would be required to explain why they have not included such information, in the first attempt to legally impose such a “comply or explain” regime on larger companies.

Groups that believe that the CSR proposals do not go far enough generally feel that the enforcement mechanism will be lax, and fail to hold companies to account, whilst business interests say that the Commission has proposed a “comply or explain” system different in nature from previous examples (see background).

A surprising choice of enforcement

“It’s slightly surprising that the Commission has decided to implement comply or explain into the legislation, since it is usually used for voluntary codes,” said John Davies, the head of technical issues at the Association of Chartered Certified Accountants.

“Indeed where ‘comply or explain’ is currently used in European rules, the Commission itself has acknowledged that these procedures can be unsatisfactory because they can produce sketchy results and be uninformative,” Davies added.

The enforcement mechanism came in for heavy fire from the European Coalition for Corporate Justice (ECCJ), an NGO, in response to the proposals.

A statement from the group said that “comply or explain” leaves excessive discretion to companies to decide what they report on, and how they report, adding: “We don’t believe such approach will make the legislative reform achieve its objectives.”

“The ‘comply or explain’ approach won’t ensure robust reporting, true identification of significant risks and impacts companies have on society, comparability of the information and enforcement,” said Jérôme Chaplier, the ECCJ coordinator.

Industry fears the new approach

But businesses believe that the new regime would offer a different kind of “comply or explain,” one that goes further than before.

A source close to major European companies, who preferred to remain anonymous, said that in Denmark – one of the countries that uses such an enforcement regime – there is a broad understanding of what it means: businesses can explain where they do have policies but prefer not to disclose them.

“In the Commission proposal the issue is much more prescriptive. Companies that have policies but do not want to report them in respect of certain areas – like human rights or anti-corruption – ought to be able to explain why. If you have a policy under the Commission proposals, you have to comply and disclose,” said the industry source.

The Danish example

For the ECCJ’s Chaplier, Denmark is not a shining example. “Danish companies don’t address difficult human rights or environmental dilemmas and supply chain issues - for which they are desperately seeking to avoid responsibility,” he said.

Ironing out the fine print on how the “comply or explain” system works is likely to be one of thornier issues as the draft rule changes make their way through the Parliament and the Council.

The Commission itself acknowledged in presenting the proposals that: “Different stakeholders have different views on what ‘comply or explain’ legislation should look like. Jurisdictions claiming that they have a “comply or explain” approach to transparency often have very different legislation.”

The EU executive insists that its “comply or explain” system will be clear and flexible, but others are less convinced.

“Further guidance is necessary to reduce any misinterpretation of the new requirements… The EU now needs to provide information as to how such measures will be enforced, and what would be the consequences of non-compliance,” said Rachel Jackson, ACCA’s head of sustainability.

Jackson said there needs to be a debate on the issue, and it will be discussed at a round-table in the Parliament on 4 June by members of the Corporate Sustainability Reporting Coalition (CSRC).

Parliament will debate “comply or explain”

The CRSC represents financial institutions, professional bodies, NGOs and investors, and will be co-hosted at the round table by MEPs Raffaele Baldassarre (Italy; European People’s Party) and Richard Howitt (UK; Socialists and Democrats).

It will be the first time the issue is aired in Parliament, where all sides of the argument debate what the “comply or explain” regime might look.

“Although Commissioner Barnier has indicated that he favours a flexible and unburdensome regime, the Parliament may look to strengthen the requirements regarding the explanations companies must give if they do not comply,” ACCA’s Davies said.

UK threatens firms with gender quotas as women's appointments fall

The British government, which has staunchly opposed EU efforts to set gender quotas for corporate management, has warned it could introduce quotas if British companies fail to appoint more women to their boards.

The move could give renewed impetus to the gender quota proposal launched last November by EU Justice Commissioner Viviane Reding, which was heavy criticised by Britain.

"Companies should be under no illusion that [the UK] government will adopt tougher measures if necessary," UK Business Secretary Vince Cable told the daily Standard on 10 April.

"Quotas are still a real possibility if we do not meet the 25% [UK] target," Cable added.

The warning came in the wake of a report also published last week indicating that the pace of women's appointments to UK boards is slowing.

UK appointments for women fell off last year

Published by the Cranfield School of Management, the report found that during the second half of last year the number of women appointed to boards of the 100 largest listed UK companies fell from 44% to 26%, whilst female appointments to the boards of the next 250 largest UK listed companies also fell from 36% to 29%.

Cable said UK ministers continued to believe a voluntary led approach was the best way to bring equality, but threatened companies with "tougher measures" – and quotas – to force women on to boards if firms would not appoint them voluntarily.

Reding proposed legislative action on gender quotas for corporate boards after her calls to take voluntary steps to increase the number of women on boards to 40% by 2020 failed to deliver tangible results.

Her draft directive set the objective of achieving 40% women in non-executive board-member positions in publicly listed companies, with the exception of small and medium enterprises.

Targets should be reached by 2020

Companies with fewer than 40% of women in such positions would be required to make appointments by applying clear, gender-neutral and unambiguous criteria, and to prioritise the appointment of women where candidates are equally qualified.

Such a rule would aim to reach the 40% target of women in non-executive positions by 2020 for private companies, whilst public undertakings would be expected to reach the target more quickly, by 2018.

Companies would face fines and other sanctions for failing to comply.

Cable's warning suggests that the UK could modify its strong resistance to Reding's proposal.

Parliament backs Commission plan

On 13 March the European Parliament backed the Commission's pledge to create binding rules to increase the number of women in top jobs, if member states have not voluntarily taken action to redress gender imbalance in the workplace.

Even though some European countries - including Belgium, France, Italy, the Netherlands and Spain - have set targets for corporate boards, Britain and Sweden have led the charge against introducing quotas.

One of the Cranfield report's authors, Susan Vinnicombe, said: "At Cranfield we have stood steadfast against quotas on the basis that chairmen must understand the benefits of gender diversity and commit to achieving it."

She said that Reding's proposal would be the only alternative if companies continued to ignore voluntary measures.

"Unfortunately, too many chairmen choose to ignore the issue in the false hope that it will go away. Viviane Reding's demanding legislation is on its way and it goes far beyond [UK] recommendations," Vinnicombe said in a statement on 11 April.

She added: "It is becoming a matter of urgency for those companies that do not have a gender balanced board to let go of their board stereotypes and appoint more creatively."

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