HOW TO STRENGTHEN THE STAKEHOLDER VOICE

05 October 2017 by Chris Hodge

New guidance from ICSA and the Investment Association will help organisations to engage meaningfully with their stakeholders.

In its response to the green paper consultation on corporate governance reform published in August, the government highlighted the new guidance on stakeholder engagement, produced jointly by ICSA and the Investment Association, as one example of the industry-led action needed to complement its proposed regulatory reforms to bring about better governance.

Titled 'The Stakeholder Voice in Board Decision Making', the aim of the guidance is to help boards think about how they understand and weigh up the interests of their key stakeholders when taking strategic decisions.

We hope that it will be of use to the boards of all companies – whether listed or privately owned and irrespective of their size or sector – and potentially for other organisations too.

Assisting boards

There were two related reasons we decided to produce the guidance, both stemming from the recognition that – whatever one's views on the specific proposals that were put forward – the government was right to highlight the relationship between business, its stakeholders and the society in which it operates as an issue, and to put that high on businesses' agendas.

First, it was clear from talking to companies that many acknowledged the issue needed to be higher on their agenda.

It was also clear that many companies, including those already making concerted efforts to engage meaningfully with their stakeholders, were looking for some assistance. This was the main reason we decided to develop guidance on the subject.

We were pleased that the Investment Association agreed to partner with us to produce the guidance. Although some commentators have characterised this debate as being 'shareholders versus stakeholders', in reality there is a lot of mutual interest.

As Chris Cummings, CEO of the Investment Association, puts it: 'Investors want companies to take decisions which will generate the best long-term value to their shareholders. To make such decisions, boards need to hear and take account of the views of the stakeholders. Failure to do so could impact on the future success of the company.'

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In the process of researching and testing out the guidance, we spoke to many companies, investors, stakeholders, representative bodies and NGOs.

We learnt a huge amount from their insights and experience, which hopefully is reflected in the guidance. We also found that there is already a lot of good practice out there from which other companies can learn.

Although welcoming this debate that the government initiated, we were keen it should not come to be defined as a choice between the specific options that were put forward in the green paper – namely stakeholder representatives on boards, designated non-executive directors, and stakeholder advisory panels.

That is not to denigrate those approaches in any way. All of them can be a useful and effective means of ensuring that the board's decisions are informed by an understanding of the impact on stakeholders, and all are covered in the guidance.

But they are not the only ways of doing that and, importantly, their impact will be limited unless the company's systems and culture support them. The same is true of any other single action the company might take.

The second reason for producing the guidance, therefore, was to encourage companies to think about these issues in a systematic way. It is designed to help boards think through the elements that might be involved in understanding and assessing the impact on key stakeholders.

What it does not do is attempt to tell them what the right way of doing so is; that is something only the board can determine.

Six sections

The guidance starts with a set of principles (see box on page 28) that we believe are generally applicable to all organisations. Most of them ought to be self-evident, but can be overlooked – for example, the need to choose engagement mechanisms that work equally well for both the company and the stakeholders concerned.

After a brief reminder of directors' general duties as set out in the Companies Act 2006, the guidance is divided into six sections:

Stakeholder identification

There are many groups that a company will interact with, or are directly or indirectly affected by the company's activities. Boards need to have a framework for defining and identifying key stakeholders, so that they have a clear and justifiable basis for prioritising between them.

This section of the guidance suggests ways in which they can do so and emphasises that this should not be thought of as a one-off exercise. Priorities will change.

Board composition

This section explores two different approaches that boards could consider if they conclude they lack sufficient knowledge and understanding of the interests of the stakeholders around the boardroom table.

One is to reserve one or more board positions for directors drawn from a specific group of stakeholders, such as the workforce. The other is to extend the selection criteria and search methods for all non-executive directors to identify individuals with relevant experience or understanding.

Induction and training

Directors rarely join a board 'fully-formed', with all the knowledge and expertise they need to carry out their role.

This section highlights that understanding of the company's key internal and external stakeholders should be an integral part of the induction process and any ongoing development programme, and identifies ways in which this can be done.

Board discussions

Most boards suffer from a shortage of time and an excess of information. This section aims to help them think about how they can make best use of both.

It deals in turn with: the management of the board's agenda; the form and frequency of the information the board wishes to receive; and whether any individual directors or board committees should have specific responsibilities for some stakeholder-related issues.

Engagement mechanisms

Although there will be cases where the board feels it needs to engage directly with certain stakeholder groups or on certain issues, most engagement will take place at the operational level.

This section therefore covers the desirability of the board having an overview of overall engagement, so that it can decide whether it is sufficient and appropriate, as well as some of the specific mechanisms companies use to engage with their stakeholders, such as advisory panels.

Reporting and feedback

This section considers both how companies can report to shareholders through the annual report, and how they can establish feedback mechanisms with their other stakeholders.

One of the points emphasised most frequently in our discussions with stakeholders was that engagement must be a two-way process if it is to succeed in establishing a degree of trust between the company and its stakeholders.

Not the end

In August, shortly before the guidance was finalised, the government announced that it would introduce new regulations to require all companies of a significant size to explain how their directors comply with the requirements of section 172 of the Companies Act 2006.

The intention is that this regulation will come into effect by June 2018. If necessary, the reporting section of the guidance will be updated then to reflect the regulations.

"ICSA does not see the publication of the guidance as the end of our interest in this issue"

Other parts of the guidance may also need to be updated as a result of the reforms announced by the government.

For example, the Financial Reporting Council has been asked to consult on possible changes to the UK Corporate Governance Code, including one that would require listed companies to have either a designated non-executive director, a formal employee advisory council or a director from the workforce, or to explain why not.

In any event, ICSA does not see the publication of the guidance as the end of our interest in this issue.

We are developing a section of the ICSA website that will include links to other sources of advice, case studies showing how some companies have introduced policies and processes intended to bridge the divide between the company and its stakeholders, and other resources.

We will regularly review the guidance to make sure it is meeting its purpose of assisting boards to develop their own bespoke arrangements for engaging with and taking account of their key stakeholders.

Credit: Chris Hodge is policy advisor at ICSA: The Governance Institute