

**SEMINAR – THE RESPONSIBILITY DIRECTION AND LEADERSHIP OF  
CORPORATIONS – NOVEMBER 2007 – ÉVORA**

“The values Dilemma of Corporate Governance”

**(1) Scope of the debate**

*“What is an ultimate goal of a Corporation and how should Corporate Governance play a role on it”*

**(2) Value elements to be considered on the ultimate goal of a Corporation**

- Value creation for **shareholders**
- The “right” level of satisfaction of **client needs**
- Sustainability on the long term, which should include the interactions between the **Company and its environment**.

And, how can a Corporation be sustainable in fulfilling its goals (whatever they are) if the surrounding Society faces cultural, social and economic degradation. It is conceivable to consider brilliant,

flourishing Corporations as isolated islands of a degrading Society?

So a Corporation needs to be involved on **improving Society**

(through sponsoring of **charity; education, arts, sports**, etc....)

- Keep employees **happy** and **motivated!** Remember that a Corporation's performance is the combined output of all its **employees.**
- Human dignity! Remember that work not only fulfills one's individual needs but also is an expression of **human dignity!** Moreover: Is it not a strong enough value in order to be the ultimate value and have all the other concurring to its fulfillment?

So!

Is this range of values too broad? Who dares to exclude any of these!

Should we eventually include others we forgot?

Now we need to rank them and make them instrumental (in order to achieve the goals). How to implement them. Not only efficiently but also ethically.

**(3) Who has the mandate to identify, select and rank Corporate Values? And control execution? (we reach the core of Corporate Governance issues)**

- Perhaps 1<sup>st</sup> of all we should clarify **who has the mandate**:  
“GOD?”  
“A Superior Order of things?”  
“The Cultural framework” where the Corporation acts?”  
“The Shareholders?”  
“The Board of Directors?”  
“The Ceo?”
- Now we enter the World of the “**Agency problems of Governance**” of Corporations.
- Even if we lead aside the quest for a “Supernatural Order” and we accept that the fingerprints of the values are embedded on each of us, therefore admitting different values and different behaviors, we still need to solve the **Corporate Governance issues** on a practical way.

And now we come into trouble:

Under the scope of defining and implementing a “socially responsible” policy and enterprise culture, I have seen the most striking **abuses and nepotistic practices**.

- Do we agree (on a public Company) that Shareholders consider the set of values and culture (and its reflexes on the performance and success of the Company) when they buy shares in a company? And therefore they **should not be asked to have a say on its definition**. Not even on its ratification? (Please consider they can be called to decide and after sell the shares next day).
- How should the values and culture of an organization be defined? Just recognizing the legacy and make it modern and “politically correct”? How? Bottom up? Top down?
- Is the alternative to have the CEO defining those values and culture (taking or not them into a Board debate and decision) and making their public and transparent disclose inside and outside the Company?
- Following the CEO route (I really do not see how the “legacy” one can be feasible) we are immediately under the fire of those who claim that “Managers have assaulted Companies on detriment of its real owners – the Shareholders”, coming to the central point of the big Governance problems and debate, so actual these days!

#### (4) **The Social pressure over Corporations**

- What has been said is not theoretical!

It is now assumed as part of our Civilization that Corporations do have a Social responsibility (without a consensus about its scope and Governance)!

- The United Nations has launched a global pact for sustainable organizations.
- European Union has published in July 2001 a declaration about Corporate Social responsibility.
- We have now certification for the Social Responsiveness (eg. SA-8000 – Social Accountability 8000)
- In Europe and US we have rankings about the best employers (“The best Companies to work for”).
- There are indexes to evaluate the Social performance of Corporations like the Dow Jones sustainable Indexes.
- I “googled” “Corporate social responsibility” and obtained 41.9 million references in half a second! And 2.7 million of “Corporate Sustainability! (and missed all those not using the English language).

**(5) Some outside opinions**

“The discussions of the “Social responsibilities of business “are notable for their analytical looseness and lack of rigor.

“... In so far as his (Corporate executive) actions in accord with his “social responsibility” reduce returns to stockholders he is spending their money ...”

“the executive is an agent serving the interests of his principal. This justification disappears when the Corporate executive imposes taxes and spends the proceeds for “social purposes” ... they can do well but only at their own expense”.

“... The doctrine of “social responsibility” ..... I have called it “a fundamental subversive doctrine in a free Society! ....

This was said by Friedman in September 13, 1970 (NY Times Magazine).

Charles Handy, on his article “What’s a Business for?” published December 2002 at HBR says:

“We can not escape the fundamental question, whom and what is a business for? .... the terms of business have changed. Ownership has been replaced by investment and a Company’s assets are increasingly found in its people ..... We need to rethink our assumptions about the purpose of business.”

“A good business is a community with a purpose, and a community is not something to be owned.” “..... have members and those members have certain rights...” “..... Leaders of those Companies need to bind themselves to ..... doing no harm ..... (it) goes beyond meeting the legal requirements regarding the environment , conditions of employment , community relations and ethics.”

“..... but doing good does not necessary rule out making a reasonable profit.”

Positioning himself on the opposite approach of Friedman's, Charles Handy does not give us the criteria we should use to implement his thoughts.

Let's move into Porter with his article\* "Strategy & Society" also published in HBR December 2006.

Porter tries to be more rational defining the Criteria for Corporate Social Responsibility (CSR):

"Broadly speaking, proponents of CSR have used four arguments to make their case: moral obligation, sustainability, license to operate, and reputation."

"All four schools of thought share the same weakness: they focus on the tension between business and society rather than on their interdependence".....

"Consequently none of them is sufficient to help a Company identify, prioritize, and address the social issues .... The result is .... uncoordinated CSR and philanthropic activities disconnected from the Company's Strategy."

"A Corporate Social agenda looks beyond community expectations to opportunities to achieve social and economic benefits simultaneously"

"The best corporate citizenship initiatives involve far more than writing a check: they specify clear, measurable goals and track results over time."

"Corporations are not responsible for all the World's problems .... Each Company can identify the particular set of social problems that it is best

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\* With Mark Kramer

equipped to help resolve and from which it can gain the greatest Competitive benefit.”

#### **(6) The Governance issues**

Under the debate of “Good Governance” the topic of Corporate Social Responsibility (CSR) is taking an increasing importance.

There is a clear trend to have the CSR issues becoming more and more a topic for the board room but this is not yet a standard situation. The Board is obviously influencing always the CSR agenda through its participation on Values, Strategy and Goals definition. Or through setting the remuneration policy. But a more explicit approach is being requested.

In the UK the Company law Reform White Paper of 2005 states “a Director must (so far as reasonably practicable) have referred to ..... the interests of employees, suppliers, costumers, the Community and the environment”. And “the basic goal for Directors should be the success of the company for the benefit of its members as a whole ....”

In a survey sponsored by the Canadian Cooperation Association and published in March 2005 two different approaches were detected for the role of CSR and its impact in Governance.

The most committed ones see CSR to be defined embedded with the Values discussion and definition and a CSR strategy should be seen as coexistent and coherent with the overall Strategy.

The other view considers that CSR should be discussed (being very important) at operational Risk Management level and come into the Board as part of it.

The most militant trend goes into the demand to replace the Board duties from **shareholders fiduciary** into **stakeholders fiduciary**.

Arguing that all the stakeholders put their assets at risk, at the same level that shareholders risk the financial capital.

We could even identify opinion groups and think tanks that request that all stakeholders should have representation at the Board level. Shareholders should not have more than 50% of Board representation.

## (7) **Conclusions**

So far it is not clear to me what is the right connection between “Best practice in Corporate Governance” and “CSR”.

Let's start with some preliminary ideas and beliefs – may be I should call them recommendations - based on my experience and research on this topic.

1<sup>st</sup> - Business cannot ignore (at least) “CSR” issues, neither the increasing awareness of stakeholders, and the impact it can have on business performance (not only on the long term but also on the short term). And therefore CSR is a topic to the Management team and to the Board.

2<sup>nd</sup> - The concept that Board is acting as an Agent on behalf of Shareholders – the Principal – aiming to create shareholder value, needs, at least, to be updated by revisiting the concept of shareholder value. The increasing importance of Institutional shareholders (e.g. Pension Funds; Sovereign Funds) with their own liabilities towards their participants is also forcing a different approach.

3<sup>rd</sup> - CSR will become an excuse for institutionalized nepotism, if not based on a very transparent and fully disclosed selection of values, strategy and goals. A clear Governance model should deal with the issue of CSR.

4<sup>th</sup> - Changing the concept from “shareholder value” into “stakeholder value”, while disregarding the first 2 recommendations, opens the door to arbitrary decisions that can create more harm to the Corporation long term sustainability than the traditional model Agent/Principal with a good and solid Risk Management model where the different outputs and interactions are well analyzed and managed.

Lisbon, 30 November 2007

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### **QUESTIONS FOR VOTING AND DEBATE**

1. Should Companies (publicly or privately owned) have a “Corporate Social Responsibility” – CSR – police and practice?
  - (1) Yes! Clearly
  - (2) No!
  - (3) It depends!
  
2. Should Companies (publicly owned) have a “Corporate Social Responsibility” – CSR police and practice even at the expenses of shareholder value?
  - (1) Yes! Clearly
  - (2) No!
  - (3) It depends!
  
3. Should Boards fiduciary obligations move from shareholder value into “stakeholder value”?
  - (1) Yes! With representatives of different stakeholders.
  - (2) Yes but just with shareholder representatives and Independent members

(3) No! I prefer the mode Agent/Principal on behalf of shareholders.

## **Resources**

“The Social Responsibility of Business is to increase its Profits” by Milton Friedman, September 13, 1970. The New York Times Magazine.

“Rethinking the Social Responsibility of Business” a Reason debate featuring Milton Friedman, John Mackey and T.J.Rodgers. October 2005.

Reason line.

“What’s a Business for? By Charles Handy December 2002” HBR

“Strategy & Society. The link between Competitive Advantage and Corporate Social Responsibility” by Michael Porter and Mark R. Krame. December 2006. HBR.

“The Stakeholder Fiduciary: CSR, Governance and the future of Boards” by Allen L. White, senior advisor. BCR April 2006

“The Convergence of Corporate Governance and Corporate Social Responsibility” by Coro Strandberg. Cosponsored by Canadian Cooperate Association” March 2005.

“Ética-Factor de Realização e Progresso” – ACEGE, Outubro 2004

“Global Corporate Governance Guide 2004 – best practice in the boardroom”, by  
Globe white page Lts., 2004