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Essay

Sustainable business leadership – take it from the top

By David Grayson and Andrew Kakabadse

Board directors should take the lead in ensuring sustainability is the focus across businesses

In well-run companies, boards approve and regularly review strategy, assess performance on implementation of the strategy, hold the executive to account, ensure effective succession-planning for themselves and senior management, and set overall values and culture. New research from Cranfield's Doughty Centre and Business in the Community shows the range and distribution of governance models for sustainability and responsibility in the UK's leading companies (FTSE 100 companies and Corporate Responsibility Index top performers), as well as giving insight from interviews with executive and non-executive directors.

Boards should be critical to embedding corporate responsibility and sustainability (CR&S). This has been recognised by chief executives of companies committed to corporate sustainability, interviewed in the 2010 Accenture/UN Global Compact CEOs' survey. It found that 93% of chief executives say boards should discuss and act on issues of social, environmental and governance performance (up from 69% in a similar survey in 2007). In the same survey, 75% say their boards are discussing CR&S (against 45% in 2007 – one of the steepest increases in activity that the survey shows).

In the Accenture/UNGC survey, 96% of the respondents believed that environmental, social and governance issues should be "fully embedded into the strategy and operations of a company" and 81% felt that they had already done this in their organisations.

However, as the author of the 2007 and 2010 surveys, Peter Lacy, argued in his October 2012 Ethical Corporation essay, business leaders may not yet fully appreciate the business transformation that sustainability requires.

"From my own experience covering more than a decade of working with many of the leading companies in the world on this agenda, at a guess, I would say that less than 1% or 2% could honestly say that they have fully integrated sustainability into strategy and operations, and those companies – the real true north innovators and leaders – probably wouldn't make the claim because they know what it means and that it's a journey of continuous improvement and renewal."[1]

Chief executives may, therefore, hold a genuine but exaggerated sense of how far they have yet embedded sustainability – including into corporate governance – because they are yet to appreciate the true extent of the change to business and business models that sustainable development requires.

Governance models in use

Our research suggests that most large, UK-headquartered companies do now have some form of board oversight of their commitment to CR&S. There are a number of different models for board oversight and governance of CR&S. These are:

1. **Formal dedicated corporate responsibility and sustainability or similarly titled committee of the board** – where all the members are board members (this may include some executives if they are also board members). In 2012, National Grid replaced its existing risk and responsibility board committee with a new committee, chaired by Philip Aiken, for safety, environment and health. Also in 2012, Tesco created a board-level corporate responsibility committee.

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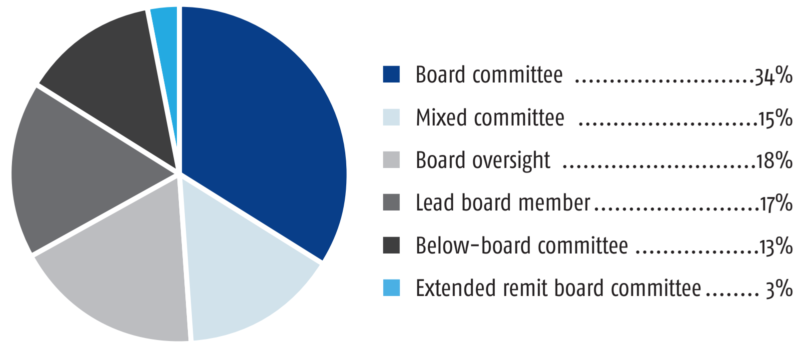
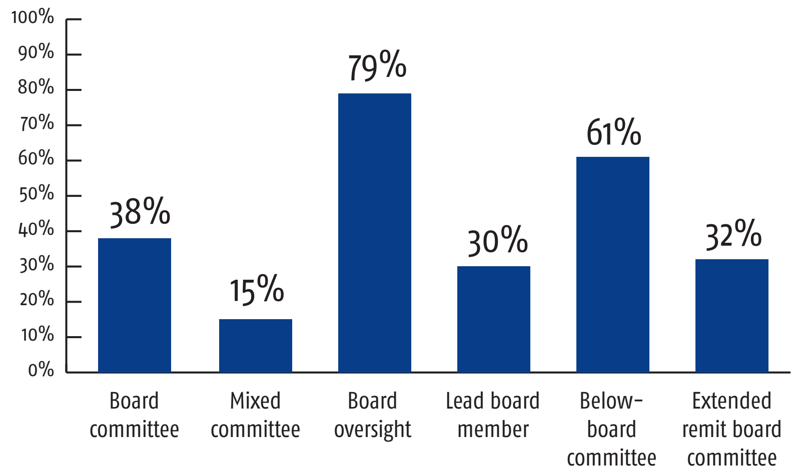
2. **Mixed CR committee** – which includes at least one board member, as well as senior executives who are not board members. At Thames Water, the health, safety and environment committee advises the board on any significant matters relating to CR&S. It consists of both non-executive directors and operational directors.
3. **Reserved to board** – there is an explicit statement that issues of CR&S are addressed by the board as a whole, and there is no delegation to a board committee: this is the approach of pharmaceuticals group Shire, for example.
4. **Lead board member(s)** – a board member (usually a non-executive director) is publicly designated as the lead director for CR&S (a variation is where several board members are each given a lead responsibility for a particular aspect of CR&S such as climate change or health and wellbeing). Dame Nancy Jane Rothwell is AstraZeneca's lead independent non-executive director for corporate responsibility.
5. **Below-board CR committee includes only non-board members** (excluding the chief executive). Legal & General's corporate responsibility committee is chaired by the chief executive and includes other executives.
6. **Explicit extension of the remit of an existing committee of the board such as audit and risk** – all the members of this committee are board members (which may include executives if they are also board members). Burberry is an example.
7. **Company explicitly makes no provision** – no company in our research fell into this category and this is, therefore, left out of the subsequent analysis.

Principal governance mechanism for corporate responsibility and sustainability in the FTSE 100



Looking at all the governance mechanisms in use in the FTSE 100 companies:



Sources: Boardex, CRI submissions, CR reports and corporate websites

In practice, these models are not generally mutually exclusive: some companies employ several of these models simultaneously. This may involve a specific board committee as well as regular, full board discussion, extended remit of an existing committee (usually audit and risk), and a more operational committee below the board.

The following statistics, therefore, are a snapshot in autumn 2012. They are based on our interpretation of how the company describes board oversight and governance of CR&S, and what appears to be the main model in use in that company. The figures relate specifically to the FTSE 100.

Almost half of the FTSE (49%) use a dedicated board committee, composed either exclusively of board members (34%) or a mixed committee with some board members and some non-board members (15%). Just under one-fifth (18%) reserve discussions to the board as a whole; 17% rely on a lead board member; 13% on a committee immediately below the main board and 3% have extended the remit of an existing board committee.

These UK results are broadly similar to international practice. In a UN Global Compact survey in 2010, the three models that are encountered most frequently among signatory companies are: first, tasking the entire board with oversight; second, creating new committees dedicated exclusively to sustainability; and third, using existing committees that assume responsibility for sustainability as one aspect of their activities[2].

In practice, we suspect that, longer term, the particular board structure is less important than the mindset with which the board approaches sustainability. In the short to medium term, there is probably value both in a board committee (whether extending the remit of one of the existing committees or a separate sustainability committee) and regular discussion in the full board.

The UN Global Compact report states: "The breadth of challenges requires both means of oversight. Where there is no full board oversight, several things fail to happen: a) sustainability issues are not addressed in annual meetings and annual reports and b) no criteria or performance measures are set. At the same time, sustainability subcommittees of the board can be effective because they will meet

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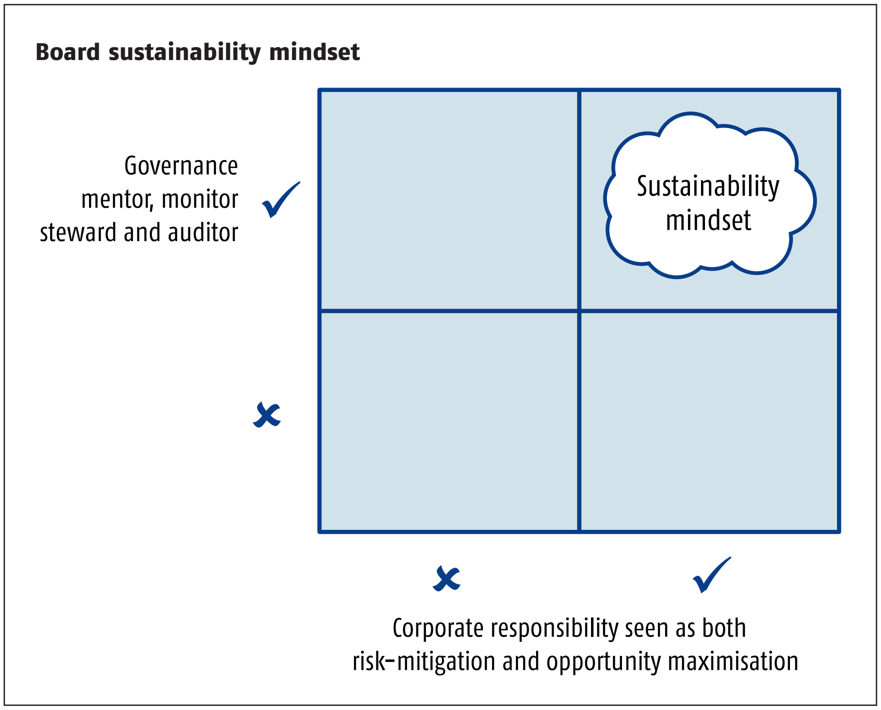

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and deliberate for longer periods of time, and then distil information for the full board."

We share this view and that of Aron Cramer, chief executive of the corporate responsibility coalition Business for Social Responsibility (BSR), who has written: "Ideally, dedicated board committees would be seen as redundant in a decade's time … but they might be needed now to catalyse the transition."[3]

Stakeholder and expert panels

A significant number of companies supplement board structures with formal, standing or ad-hoc, stakeholder-engagement mechanisms – including in some cases, a stakeholder and/or external sustainability experts panel to advise the board and/or the chief executive and senior management team.

At Unilever, for example, the board, the board CR committee and the executive have a number of sustainability advisory panels including an external group of five "independently minded experts who guide and critique the development of our strategy".

For many companies and boards, however, there is still a critical mindset shift that has to occur, and goes back to Peter Lacy's argument in True North. This shift can be summarised in the now famous formulation of Collins and Porras in their book Built to Last.[4] Namely, the shift from the tyranny of the "or" to the genius of the "and".

Specifically, on the concept of governance, the shift from the idea of boards as mentors or monitors, stewards or auditors, to mentors and monitors, stewards and auditors. And a second shift from the idea of CR&S as being about risk mitigation to the recognition that to be truly embedded, it has to become both risk mitigation and opportunity maximisation. Business school professors are allegedly fixated on their 2x2 matrices. At the risk of reinforcing stereotypes, therefore, we might express the board sustainability mindset as a 2x2 matrix where one axis represents the attitude to governance, and the other axis represents attitude towards sustainability (see graphic left).

The board sustainability mindset, therefore, can be defined as: "A collectively held view that long-term value-creation requires the company to embrace the risks and opportunities of sustainable development; and that the board are simultaneously mentors and monitors, stewards and auditors of the management in their commitment to CR&S."

Our qualitative research suggests that currently, CR&S leadership and stewardship, if it exists, tends to come from the chairman or chief executive or another board member, rather than yet being a collective mindset of the board as a whole.

It is not surprising that this either/or mindset prevails within companies when it comes to CR&S. This polarity of "mentors or monitors, stewards or auditors" has dominated corporate governance literature for several decades. While there are operational improvements to the practicalities of board oversight of a company's commitment to CR&S, the crucial change is this mindset shift among the board and senior management team, to emphasise that the board are mentors and monitors, stewards and auditors for CR&S.

Similarly, while concepts of CR&S have become more common in recent years; in practice, companies remain at very varied stages of corporate responsibility maturity; and the idea that the commitment to CR&S should be a driver of, and a consequence of, an opportunity-maximisation strategy remains relatively new.

CR&S goes across everything. There is an analogy with change-management: it can be the equivalent of appointing a change-management director and thinking that they will take charge of change and the rest of the organisation does not need to worry about it. CR&S has to become like finance: it would be a very foolish non-exec who does not understand the basics of finance and the finances of the business on whose board he or she serves.

Achieving this sustainability mindset shift cannot be legislated for. It can only occur through sustained and open dialogue among the board and senior management team, until there is this consensus about the link between sustainability and long-term business survival and success. In practice, companies are at different stages of corporate responsibility maturity. Depending on the current stage of maturity, there are different board engagement techniques that a chairman or chief executive or chief sustainability director might employ.

Some boards have used discussion of future


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Sustainability is now part of the big decision process

scenarios, or participation in an external initiative such as BITC's Visioning the Future – Transforming Business programme, or a corporate crisis to trigger such a mindset shift. Kingfisher ran a youth board for a year with senior directors mentoring the young people and briefing them on the business and strategic options etc. United Utilities brings the voice of younger employees into its board's corporate responsibility discussions.

If such a mindset shift occurs, there are a number of good practices that will enhance board effectiveness. Without the mindset shift, the collective good practice identified through our research may bring marginal, positive impact, but will not transform the organisation's culture and practice.

Recommendations for boards

We believe that corporate boards should now:

1. Assess whether they have a sustainability mindset and, if not, identify how to help create this.
2. Periodically evaluate whether their current model for board oversight and governance is fit for purpose; and also whether existing board committees are effectively incorporating CR&S within their remit.
3. Review their board skills matrix and whether this reflects the company's commitment to CR&S.
4. Ensure that CR&S is effectively incorporated into induction and continuing professional development for board members; and in the annual appraisals of board effectiveness with specific questions.

Boards play a critical role in the long-term success of companies. As corporate responsibility and sustainability becomes a business-critical issue, it is imperative that board members understand their role in providing effective oversight and governance of commitments, and are properly equipped to carry this out. ■

1 Where is 'true north' for sustainable business? Business needs to accelerate the shift from incremental to transformational change, Peter Lacy, Ethical Corporation Oct 2012.

2 Retooling the Boardroom for the 21st Century, panel discussion at US Global Compact Network Symposium, San Francisco, October 19 2009.

3 Giving Sustainability a Seat In the Boardroom, Aron Cramer, BSR, GreenBiz April 20 2011.

4 Built to Last, Collins and Porras, 1994.

David Grayson is professor of corporate responsibility and director of the Doughty Centre for Corporate Responsibility and Andrew Kakabadse is emeritus professor at Cranfield School of Management. This essay is abridged from a report they have authored with Business in the Community on how boards organise governance and oversight of corporate responsibility. The full report is available at www.bitc.org.uk