OUR MISSION:

The Global Corporate Governance Forum is an International Finance Corporation (IFC) multi-donor trust fund facility located within IFC Advisory Services. The Forum was co-founded by the World Bank and the Organisation for Economic Co-operation and Development (OECD) in 1999. Through its activities the Forum aims to promote the private sector as an engine of growth, reduce the vulnerability of developing and transition economies to financial crisis, and provide incentives for corporations to invest and perform efficiently in a socially responsible manner.

The Forum sponsors regional and local initiatives that address the corporate governance weaknesses of middle- and low-income countries in the context of broader national or regional economic reform programs.

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Global Corporate Governance Forum

Foreword by Peter Zollinger

Governance Practices
and the Board: Integrating Best
Stakeholder Engagement
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DISCLAIMER

This publication is an attempt to assess and explain the universe of issues and challenges facing boards and companies in the area of stakeholder engagement. It is not a formal position or expert opinion on this topic. A list of resources and expert sources is offered. However, readers are advised to seek professional expertise or is not a formal position or expert opinion on this topic. A list of resources and expert sources is offered. However, readers are advised to seek professional expertise or guidance to design or implement stakeholder engagement initiatives. We also wish to provide special thanks to Peter Zollinger, Senior Vice President, SustainAbility, for writing the Foreword, and to Mervyn King, Michael O'Sullivan, and Bonny Thebenyane for their insightful comments.

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Three often found misconceptions in business can be summarized as follows (and I admit, somewhat provocatively): First, the term stakeholder is seen as a euphemism for polarizing, anti-business campaigners (read troublemakers). Second, stakeholder engagement is for companies that are aspiring for political correctness (at best) and risk to hand the steering wheel to groups that have little legitimate voice (at worst). And third, there are no real-life connections between best practice corporate governance and stakeholder engagement.

This FOCUS Publication effectively dispels these misconceptions and presents a structured and practical case for stakeholder engagement as a means to business success and societal trust.

More and more business leaders recognize that their traditional management recipes are providing insufficient guidance on how to handle changing societal expectations around the globe. Frequently, reputable companies are caught in what appears to them to be a surprise controversy, despite professional public relations work and elaborate mechanisms of internal control. It should raise an alarm bell if company executives have to admit ever that they were surprised by the level of negative publicity. Have their internal radar systems been insufficiently tuned? Or has the internal escalation of warning signals failed?

'No surprises' is one of the most important principles of good corporate governance. This report explains how systematic stakeholder engagement enables both the supervisory body and the executives in any corporation to be prepared to detect, assess and manage any change in their global societal environment that may prove to be critical for strategy and their capacity to implement it. The report does not call for additional functions to be taken over by boards. Rather, effective corporate leadership involves the integration of stakeholder engagement within the accepted core functions of boards as part of best practice corporate governance. Such core functions include policy setting, accountability and control, and the selection of executive management.

But beyond managing risk, the champion’s league of stakeholder engagement is to embed openness and collaboration in a company’s approach for innovation. More and more new business models live off what some call strange bedfellows.
novel partnerships between business, NGOs or governments to deliver new services or come up with new products.

At the beginning of any company successfully embracing stakeholder engagement, the following are the key needs.

1. Stakeholders need to be recognized by the company as a core component of the organization's value.
2. The engagement process needs to be established as a core component of the organization.
3. Novel partnerships between business, NGOs or governments to deliver new services or come up with new products.

Peter Zollinger
Senior Vice President
SustainAbility
Companies have always had relationships with their stakeholders, which include shareholders, customers, suppliers, employees, regulators, and local communities. In fact, it would be difficult for a company to stay in business if it did not operate with the interests of these key groups in mind. When engaging with its stakeholders, a business is acknowledging that it is an interdependent entity, which is impacted by and has an impact on many different groups. For many companies, however, finding the right approach to stakeholder engagement and tapping the wider benefits it offers to their business is still uncharted territory. This FOCUS Publication provides an introduction to stakeholder engagement from the perspective of internationally recognized, good corporate governance practices. It is aimed at senior executives and company directors and explains how stakeholder concerns can inform and enhance the risk management and wealth creation responsibilities of boards of directors. It provides practical tips and tools to help navigate stakeholder engagement in a way that strengthens the long-term sustainability of companies and enhances trust and reputation among stakeholders.

"Our stakeholders are our business."

Standard Bank • 2005 Annual Report
Stakeholder Engagement and the Board: Integrating Best Governance Practices

Most companies communicate with stakeholders, providing information about the organization and its products, services, and operations to shareholders, customers, suppliers, employees, and other groups. Effective stakeholder engagement is also characterized by dialogue—a two-way process.

Moving toward a stakeholder-conscious governance model, with broader input and ongoing engagement, is an important part of doing business. Stakeholder engagement has become an essential part of modern business, and supply chain risks have become increasingly globalized. The number and variety of stakeholders impacted by individual companies has grown, and the need for stakeholder engagement is therefore an important management issue for any company and management team. Over time, the concept of corporate social responsibility has evolved, and stakeholder engagement has become an important part of anticipating business opportunities and risks.

Stakeholders can have economic, social, or even political effects on a company, and there are many good strategic and operational reasons to engage with them. The strategic importance of stakeholder engagement and the strategic importance of stakeholder engagement are also interrelated. The process of communicating with these groups is one type of stakeholder engagement, and customers, stakeholders, providing information about the organization and its products, services, and operations to shareholders.

"Every decision the Board makes takes into account the needs and expectations of all our stakeholders."

BHP Billiton • 2007 Annual Report
Experience shows that trust and relationships take time to build but are valuable assets. To build trust, the company must show it has listened and acted in response to stakeholder concerns. This is why ongoing communication with and reporting back to stakeholders is such an important component in any engagement strategy. Ultimately, stakeholder engagement should become a core value for the business, managed as a business function with clear objectives and lines of responsibility. The following chapters show how this approach fits with the leadership responsibilities of boards. In particular, chapter IV provides practical tips for prioritizing stakeholder interests and successfully managing stakeholder engagement.
II. STAKEHOLDER ENGAGEMENT AND CORPORATE GOVERNANCE

Corporate governance refers to the systems by which companies are directed and controlled. The structure and operation of the board of directors, financial reporting, transparency and audit, separation of powers and minority shareowners’ rights are integral to the corporate governance system. Corporate governance is also increasingly recognized as a means to address the converging interests of competitiveness, corporate citizenship, and social and environmental responsibility, and as a mechanism for encouraging efficiency and combating corruption (King Report, 2002).

Weak corporate governance systems that lack transparency and protection for minority shareowners’ rights have been shown to reduce foreign investment and capital flows to developing economies. At the company level, good governance practices have been found to be associated with creditworthiness and higher average annual total returns (Brown, Muchin and Rosenman, 2004). Good corporate governance systems that lack transparency and protection for minority shareowners’ rights have been shown to reduce foreign investment and capital flows to developing economies. At the company level, good governance practices have been found to be associated with creditworthiness and higher average annual total returns (Brown, Muchin and Rosenman, 2004).

There are a number of different codes or sets of principles for good corporate governance. Many highlight the importance of stakeholders to good governance. One such example at the global level is the OECD Principles of Corporate Governance. The core values of the OECD corporate governance principles are:

I. Rights of shareowners and their protection
II. Equitable treatment of all categories of shareowners
III. Role of employees and other stakeholders
IV. Timely disclosure and transparency of corporate structures and operations
V. Responsibilities of the board towards the company, shareowners and other stakeholders

These principles underpin the development of a strong governance framework that, in turn, supports the development of sound capital markets.

Governance

II. STAKEHOLDER ENGAGEMENT AND CORPORATE GOVERNANCE
Definitions of Stakeholder Engagement

The term "stakeholder" has been used since at least the 1930's, when a Harvard Law Professor, E. Merrick Dodd, publicly supported the identification of four major groups of business stakeholders: shareowners, employees, customers and the general public (Preston & Sapienza).

A 1963 internal memo at the Stanford Research Institute used the term to refer to "those groups without whose support the organization would cease to exist." By definition, stakeholders have a stake in the organization, and the responsibilities of companies are to respond to them. In "The Stakeholder Fiduciary: CSR, Governance and the Future of Boards," Allen White of the US-based organization Business for Social Responsibility (BSR) has broadened attention on corporate social responsibility around corporate stakeholder engagement.

The more recent surge in interest in corporate social responsibility may have different stakeholder groups. Different divisions of operational entities differ, and in large organizations, stakeholders of each division and organization are non-governmental organizations. The supplier’s financiers, employees, customers, and local and central governments, communities, local elected officials, and the efficient use of resources and their beneficial distribution among the beneficiaries of technology and products of the organization. Some types of stakeholders are shareholders, customers, employees, suppliers, financiers, and local governments.

Corporate Governance is concerned with holding the balance between economic and social goals and between individual and communal goals. The framework is there to encourage responsible and accountable corporate governance, and the efficient use of resources and the efficient distribution among the beneficiaries of technology and products of the organization. Some types of stakeholders are shareholders, customers, employees, suppliers, financiers, and local governments.

The organization would cease to exist if these groups without whose support the organization would cease to exist. The term "stakeholder" has been used since at least the 1930's when a Harvard Law Professor, E. Merrick Dodd, publicly supported the identification of four major groups of business stakeholders: shareholders, employees, customers, and the general public. (Pressenza).
The concept of ‘stakeholder management’ emerged in the 1980s as a practice whereby companies recognized the interests of significant, non-financial stakeholders — those with sufficient influence and visibility to gain the company’s attention — and took steps to communicate with these groups and address their concerns, usually related to specific issues.

The broader practice of ‘stakeholder engagement’ emerged in the 1990s as it became clear that companies needed to address a wider range of stakeholder interests. Stakeholder engagement involves the company making a sincere attempt to respond to stakeholder concerns and to build long-term relationships of constructive engagement. This approach is different from public relations, which often focuses on short-term image management and crisis response.

Finally, White argues that a concept of ‘stakeholder governance’ is now emerging, which shifts the focus to how boards themselves operate and the extent to which stakeholder interests are integrated into core functions so that board decisions fairly balance the claims of all key stakeholders.

Engaging with stakeholders has governance implications because it goes to the heart of how power and authority are understood in a company. By definition, stakeholders have a stake in the company, and have the possibility of gaining benefits or experiencing losses or harm as a result of the operations of the company, and have a stake in the company, and have the possibility of gaining benefits or experiencing losses or harm as a result of the operations of the company.

The broader practice of stakeholder engagement emerged in the 1990s and addresses these concerns, usually related to specific issues. The company’s attention — and much of its public relations activity — is focused on stakeholders — those with significant influence and visibility to gain recognition. The concept of stakeholder management emerged in the 1980s as a way of engaging with stakeholders, addressing their concerns, and building long-term relationships of constructive engagement.
The terminology describing the business-society relationship has seen a slow evolution since the 1950’s with terms such as corporate social responsibility, corporate citizenship, environmental and social performance, and sustainability favored at different times. All terms speak to the role of business as providing some ‘good’ to society, which may include jobs, law abidance, or environmental stewardship. Because the emphasis is on relations with society, the stakeholder view of the company is central to most of these concepts. Companies committed to operating responsibly and sustainably need to manage social contracts and face new, good choices; i.e., law-abidance, good environmental stewardship, responsible citizenship, and community involvement. Increasingly, organizations are reconciling their corporate goals with those of their stakeholders, leading to a paradigm shift in financial and society responsibility, and increased community involvement in the decision-making process of companies to interact with their wider communities in an ethical and socially responsible manner. From a corporate governance perspective, the evolution since the 1950’s with terms such as corporate social responsibility has been slow. The terminology describing the business-society relationship has seen a slow evolution since the 1950’s with terms such as corporate social responsibility.
DEFINING COMMONLY USED TERMS: THE ROLE OF STAKEHOLDERS IN CORPORATE SUSTAINABILITY AND RESPONSIBILITY (CONTINUED)

Sustainability implies that a process or state — such as a company’s operations — should be managed in a way that it can be maintained at a certain level indefinitely. The most common definition of sustainability is “development that meets the needs of the present without compromising the ability of future generations to meet their own needs.”

Stakeholder Engagement and Sustainability

As the power of the private sector grows, it is now fairly widely accepted that businesses have responsibilities beyond making a profit and there are many good business reasons why it is advantageous for companies to ensure that business activities are ethical, responsible and environmentally sustainable.

Experiences of leading companies have shown that demonstrable commitment to values and sustainability can help companies to achieve a variety of benefits:

- Higher employee satisfaction, better employee retention, increased employee engagement, and reduced employee absenteeism;
- More sustainable energy use and waste management, or reduced costs in their operations;
- Easier recruitment and retaining of high-quality staff members;
- Be perceived as more desirable places to work and have an easier time recruiting consumer actions;
- Clean and retain loyal customers while avoiding boycotts or other undesirable

To assess the sustainability of products, services, and other activities, companies need to use social and environmental criteria as well as financial judgment. Stakeholders are likely to have varying opinions about how such criteria are measured and interpreted.

...
Stakeholder Engagement and the Board: Integrating Best Governance Practices

One among the most critical components of sustainable governance is stakeholder engagement. Companies can use stakeholder engagement to increase the credibility of their reports. Sustainable reporting is essential to maintain stakeholders' confidence and to be acting responsibly. A growing number of companies now publish annual sustainability reports to communicate about their social, environmental, and economic performance. These companies then also obtain external assurance to ensure credibility and may further reputational damage if stakeholders do not perceive it.

Ultimately, if a company’s stakeholders feel it is responsible, it will have the legitimacy it needs to manage performance. By adopting sustainable practices, businesses can create value not only for themselves but also for the broader society in which they operate. A sustainable, responsible business strategy seeks to ensure long-term business success while simultaneously contributing to economic and social development, a healthy environment, and a stable society. This strategy seeks to ensure long-term business success while simultaneously contributing to economic and social development, a healthy environment, and a stable society. The measures put into place for the broader society in which they operate. A sustainable, responsible business strategy seeks to ensure long-term business success while simultaneously contributing to economic and social development, a healthy environment, and a stable society.

Problems that affect the company as well as the local population:

- When the support of the communities where they operate and jointly solve and challenges of the industry are addressed, companies can develop discretionary standards according to their particular circumstances.

- Foresee legislation or regulation by adopting voluntary programs, aligning them
stakeholder engagement and the board: integrating best governance practices

Coca-Cola’s use of groundwater in India

More than one out of every six people on Earth live in India, yet the nation has less than four percent of the world’s freshwater resources. In the southern Indian village of Plachimada, persistent droughts have dried up groundwater and local wells, forcing many residents to rely on water supplied through a network of borewells called the Cauvery River. The village is located in the state of Tamil Nadu, which is known for its lush greenery and fertile soil. The residents of Plachimada rely on the river for their daily needs, including drinking water, irrigation for agriculture, and for industrial purposes.

In 2004, the High Court in the southern Indian state of Kerala ordered Coca-Cola to stop extracting groundwater for its bottling operations. Justice K. Balakrishnan Nair told the company that it owned the 40 acres of land where its plant stood, but the groundwater beneath the land is a national resource belonging to the entire society. The complaint against the company alleged that the water table was being drawn down by Coca-Cola, which used deep bore wells.

At the time of the ruling, large Coca-Cola customers in other parts of the world demanded that the company provide detailed explanations of its activities in India. The University of Michigan, for instance, with annual expenditures of approximately $1.3 million for Coca-Cola products in 2004, extended some contracts on a short-term, conditional basis. The university also demanded that the company provide detailed explanations of its activities in India, and that Coca-Cola adhere to a third-party, independent audit to review the company’s activities.

Following a year-long scientific study, the High Court of Kerala determined that the primary cause of the water shortage in the local area was due to reduced rainfall and that Coca-Cola had the right to withdraw and use water from the local aquifer. Despite the ruling, Coca-Cola decided not to reopen its plant in Kerala.

Stakeholder concerns.

Independent audits to review the company’s activities and to provide detailed explanations of its activities are critical to really understand stakeholder concerns. [...] Our future success depends on finding workable solutions to the challenges facing the world in which we do business.

“Through experience, we’ve learned that operating responsibly is not enough; it is also critical to really understand stakeholder concerns. [...] Our future success depends on finding workable solutions to the challenges facing the world in which we do business.”

The Coca-Cola Company

www.thecoca-colacompany.com/citizenship/stakeholder_engagement.html
In India, Coca-Cola had already begun to engage with stakeholders at the time of the court case in Kerala, and their engagement steadily increased in the years following.

The company formed an Indian stakeholder advisory board in 2003. Chaired by a former cabinet secretary, the board provides guidance on operational, environmental, and corporate governance issues in India. In its 2006 Corporate Responsibility Review, the company noted that it had increased engagement with stakeholders.

The company has taken Indian stakeholder concerns about water seriously, addressing them in two important ways. First, the company provides detailed reporting on its water consumption and actively works to reduce its water usage. Secondly, the company has partnered with government bodies and researchers, sponsoring hydrological studies to increase understanding of local water management practices. Second, the company has partnered with government bodies and researchers, sponsorship hydrological studies to increase understanding of local water management practices.

In family-owned or employee-owned companies, shareholders may be able to sell their ownership stake, a claim to any distributions of income in the form of dividends, and the right to vote in the election of company directors. These include the ability to vote in the election of company directors, a claim to any distributions of income in the form of dividends, and the right to sell their ownership stake. In this ownership model, companies are seen as another form of personal property ownership. The interests of shareholders, most academic literature on governance begins with the interests of shareholders, most academic literature on governance begins with the interests of shareholders, most academic literature on governance begins with the interests of shareholders, most academic literature on governance begins with the interests of shareholders, most academic literature on governance begins with the interests of shareholders, most academic literature on governance begins with the interests of shareholders. Shareholders also have fiduciary responsibilities to act in the best interests of the company and its shareholders. In most countries, the law makes it clear shareholders are the owners of companies, including when to elect directors and how to adopt policies. The company has taken Indian stakeholder concerns about water seriously, addressing them in two important ways. First, the company provides detailed reporting on its water consumption and actively works to reduce its water usage. Secondly, the company has partnered with government bodies and researchers, sponsoring hydrological studies to increase understanding of local water management practices.
examples, however, are exceptions. While shareholders are entitled to a return on their investment, they cannot actually do anything with any part of a company, nor do they have any expectation of doing so (Post, Preston and Sachs, 2002). Many other types of stakeholders also have interests that are protected by law. Stakeholders, for instance, may have legally binding contracts with suppliers or customers. In some countries, certain employee rights are protected by law. A company may therefore legally bind contractors with suppliers or customers in contracts. Some company obligations to investors are also legal obligations to other stakeholders.

Stakeholder engagement can help companies better understand and manage their relationships with stakeholders. Stakeholder engagement can improve relationships with stakeholders, which in turn can lead to better decision-making and improved performance. This stakeholder model of the company is built on the idea that stakeholders contribute, either voluntarily or involuntarily, to a company's wealth-building capacity. Stakeholders are either potential beneficiaries or risk bearers of company activity, and their interests should be considered by management and boards of directors. The stakeholder model recognizes that stakeholders are not just shareowners, but also include customers, employees, and the community. This stakeholder model is further illustrated in Graphic 1, which shows the multiple linkages between a company and its diverse stakeholder groups.

Some companies are managed — and it can be argued that all should be — to create wealth for and avoid causing harm to multiple stakeholder groups. Comprehensive stakeholder management and stakeholder governance requires recognizing stakeholders who voluntarily associate themselves with a company in pursuit of their own interests, such as supply chain vendors, and those that are involuntarily impacted by corporate activity, such as communities living near a company's operations. Some companies are managed — and it can be argued that all should be — to create wealth for and avoid causing harm to multiple stakeholder groups.

Stakeholder engagement can help companies better understand the interests and concerns of stakeholder groups so that they can make informed decisions about balancing the interests of all groups to which they may owe some obligation. Considering stakeholder concerns and interests can improve relationships with stakeholders, which in turn can lead to better decision-making and improved performance. This stakeholder model of the company is built on the idea that stakeholders contribute, either voluntarily or involuntarily, to a company's wealth-building capacity. Stakeholders are either potential beneficiaries or risk bearers of company activity, and their interests should be considered by management and boards of directors. The stakeholder model recognizes that stakeholders are not just shareowners, but also include customers, employees, and the community. This stakeholder model is further illustrated in Graphic 1, which shows the multiple linkages between a company and its diverse stakeholder groups.

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To some extent, the distinction between the shareowner and stakeholder models is a false dichotomy. Stakeholders and shareowners alike are searching for methods of ensuring the long-term health and prosperity of companies.

Two broad notions have been used to make the case for stakeholder-oriented governance. The first, enlightened self-interest, argues that shareowners will ultimately be better off if they allow managers to pursue long-term objectives. Because the short-term interests of stakeholders are still given priority, the supremacy of shareowners as owners of a company is not challenged. Because including objectives that are important to stakeholder groups, in this approach, the ultimate goal is better off if they allow managers to pursue long-term objectives.

Governance. The first, enlightened self-interest, suggests that stakeholders will

a) achieve similar levels of return on investment

b) achieve better overall performance

c) achieve better return on investment

d) achieve better overall performance

To some extent, the distinction between the shareowner and stakeholder models is
The second interpretation is to make companies directly responsible to a broad group of stakeholders. Sometimes referred to as a pluralist approach, this requires company boards to demonstrate that the business is operated in a way that takes the interests and concerns of stakeholders into account (Cowe, 2001).

So, what does this look like in practice? Well, companies can capture and respond to stakeholder concerns in three ways:

1. Representation of stakeholder interests.
   - The corporation involves stakeholders in the decision making process. Should be made and then makes the decisions itself.
   - The corporation engages with stakeholders to get their input on what decisions.
   - The corporation makes business decisions that take into account.

2. Enforcement of stakeholder interests.
   - Regardless of process, one also needs to consider the principles behind the decision making process. Will the corporation take stakeholder interests into account only when they have a direct influence on existing business performance? Will the corporation take stakeholder interests into account when the actions of the corporation affect stakeholders but a change will either not improve performance or make performance worse?

The disadvantage of the enlightened self-interest approach is that there are limits to the convergence between increasing profits and pursuing the interests of various stakeholders. In many cases, there may be conflicts between these objectives. Enlightened shareowner value' is a related concept commonly associated with the UK Companies Act of 2006. In addition to acting in the best interests of all shareholders, including future shareholders, the Act requires in the best interests of all shareholders include a related concept commonly associated with enlightened shareowner value.

The disadvantage of the enlightened self-interest approach is that there are limits to the convergence between increasing profits and pursuing the interests of various stakeholders. In many cases, there may be conflicts between these objectives.

Enlightened shareowner value is a related concept commonly associated with the UK Companies Act of 2006. In addition to acting in the best interests of all shareholders, including future shareholders, the Act requires in the best interests of all shareholders include a related concept commonly associated with enlightened shareowner value.
A director of a company must act in the way he considers, in good faith, would be most likely to promote the success of the company for the benefit of its members as a whole, and in doing so have regard (amongst other matters) to:

1. The need to act fairly as between members of the company.
2. Standards of business conduct, and the desirability of the company maintaining a reputation for high environmental standards.
3. The impact of the company’s operations on the community and the customers and others with whom the company’s employees.
4. The desirability of the company’s business relationships with suppliers.
5. The key consequences of any decision in the long term.
6. A director of a company must act in the way he considers, in good faith,
These various approaches demonstrate a tension between leaving it to the company's board and management to address stakeholder concerns versus ensuring that stakeholders are represented in key decision-making processes. All point to ethical as well as business reasons to balance stakeholder needs with those of shareowners, and that in fact these have areas of commonality. For instance, if customers, trading partners, and regulators favor stakeholder-oriented companies, then this will reinforce the financial return to shareowners and contribute to the long-term success of the company.

Boards of Directors and Stakeholder Engagement

While board structures and responsibilities vary according to local norms, laws, and regulations, most boards are responsible for:

1. Setting general policies and strategic direction
2. Shaping the company’s framework for accountability, control, and risk management
3. Selecting and overseeing compensation of key managers, including the CEO

The second area of responsibility is where stakeholder engagement or bringing opinions and information from outside in to bear on board leadership. The board, while responsible for ensuring that stakeholders are represented in key decision-making processes versus company's board and management to address stakeholder concerns versus leaving it to the company's board and management to address stakeholder concerns versus ensuring that stakeholders are represented in key decision-making processes.

These various approaches demonstrate a tension between leaving it to the company's board and management to address stakeholder concerns versus ensuring that stakeholders are represented in key decision-making processes.
V. Approve a policy for external reporting

VI. Integrate stakeholder issues into annual general meetings of shareowners

VII. Discuss the risks and impacts of projects and operations and provide transparent disclosure information to shareowners and other key stakeholder groups

VIII. Convene stakeholder forums and invite key stakeholder representatives to address board meetings

In addition to being an important part of corporate accountability, stakeholder engagement can provide a broader view of potential risks. Stakeholder engagement allows companies to identify and properly manage nonfinancial risks. In the related discussion of Enron, despite its unwillingness to engage in other aspects of corporate oversight, Enron's board approved a disclosure policy that ultimately contributed to a lack of transparency. The board's responsibility to oversee management and manage corporate governance risks extends to overseeing and managing environmental and social issues as well as the impact of climate change.

Of course, many so-called nonfinancial risks—such as the impact of climate change and corporate governance failures—have financial consequences. Often it is indirect consequences of nonfinancial risks that are the most difficult to oversee and manage. One example is the Enron case, where Enron's board approved a compensation strategy that ultimately contributed to a lack of financial transparency and a compensation policy that was sensitive to share price changes.

One example is the Enron case, where Enron's board approved a compensation policy that ultimately contributed to a lack of transparency and a compensation strategy that was sensitive to share price changes. The process of stakeholder engagement increases overall accountability and transparency in corporate decision-making and helps to ensure that the board is better able to represent the interests of all stakeholders.

A key element of corporate governance is ensuring the accountability of boards. Shareowners have largely been left with the role of protesting excessive pay or board compositions that do not comply with accepted guidelines. In this regard, stakeholder engagement provides a broader view of potential risks. Stakeholder engagement allows companies to identify and properly manage nonfinancial risks. In the related discussion of Enron, despite its unwillingness to engage in other aspects of corporate oversight, Enron's board approved a disclosure policy that ultimately contributed to a lack of transparency. The board's responsibility to oversee management and manage corporate governance risks extends to overseeing and managing environmental and social issues as well as the impact of climate change.

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Stakeholder Engagement and the Board: Integrating Best Governance Practices

The company’s stunning collapse was at least partially blamed on the board’s unwillingness to demand transparency and accountability and to curb excessive arrogance. Boards should consider that reputational and relationship issues are fundamental to business operations, so stakeholder engagement should be an integral part of their strategy. Just as discussions with major shareowners help a company understand how it is viewed and what investors want, engagement with other stakeholders can be crucial to helping companies understand what society expects. Engagement may produce clear financial benefits from increased staff motivation or improved reputation.

Roles and Responsibilities of Stakeholders

Stakeholders are characterized by their relationship to the company and their arising needs, interests, and concerns, which will be paramount in their minds at the start of any engagement process. However, as the process unfolds, they will soon take on a particular role with related tasks and responsibilities. The following are just some of the different roles that stakeholders can play:

- Experts, such as academics, who have been invited to contribute knowledge and strategic advice to the company’s board;
- Technical advisors with expertise on the social and environmental risks associated with particular technological and scientific developments invited to sit on scientific and ethical panels in science-based industries;
- Co-implementers, such as NGOs, who have partnered with the company to implement a joint solution or program to address a shared challenge;
- Representatives of special interests, such as employees, local communities, or stakeholders who have partnered with the company to implement a joint solution or program to address a shared challenge.

The roles and responsibilities of stakeholders have in turn become more defined, which has been said about the responsibilities of companies towards stakeholders. From increased stakeholder engagement or improved reputation, understanding what society expects, stakeholder engagement may provide clear financial benefits that can improve performance and reputation. Stakeholder engagement helps to engage with relevant institutions, bring about discussions with them, and consider alternative business strategies. Stakeholder engagement should be seen as much as fundamental as accountability and to curb excessive arrogance.
Co-monitors, such as impacted communities, that have entered into an agreement with the company in which both parties will be responsible for monitoring outcomes of the company’s sustainability projects.

In each case, stakeholders engaging with companies have an obligation to understand the company’s objectives and be well informed so that dialogue is constructive. Finding solutions that benefit everyone is only possible when stakeholders understand and appreciate the company’s objectives and to be well informed so that dialogue is constructive.

In each case, stakeholders engaging with companies have an obligation to understand, communicate sincerely and attempt to understand, not just be transparent and report on issues that impact stakeholders. Both parties have an obligation to communicate sincerely and attempt to understand, not just be informed and knowledgeable. Stakeholders can only be well informed and knowledgeable if companies are transparent and report on issues that impact stakeholders. Both parties have an obligation to communicate sincerely and attempt to understand, not just be informed and knowledgeable.
III. THE BUSINESS CASE FOR STAKEHOLDER ENGAGEMENT

Companies that excel at stakeholder engagement excel in business. The skills developed through effective stakeholder engagement are invaluable in an increasingly complex world where companies deal with many different relationships that all potentially impact their business. For businesses with diverse geographical locations, this can be particularly challenging.

Creating Value and Wealth

Organizational wealth is the cumulative result of organizational performance over time. Companies that excel at stakeholder engagement excel in business. The skills developed through effective engagement are invaluable in an increasingly complex world where companies deal with many different relationships that all potentially impact their business. For businesses with diverse geographical locations, this can be particularly challenging.

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Every company has critical stakeholders in every dimension of its critical environment — resource base, industry structure, and social and political setting. Favorable and mutually beneficial relationships through negotiated shared values with these stakeholders allow companies to create wealth, while conflict often limits or destroys wealth.

The sources of company wealth attributable to different stakeholder groups are summarized in Table 1.

<table>
<thead>
<tr>
<th>Stakeholder View</th>
<th>Industry Structure View</th>
<th>Resource-Based View</th>
</tr>
</thead>
<tbody>
<tr>
<td>Stakeholder linkage</td>
<td>Resource and sunk costs reducing government and market regulation</td>
<td>Barriers to imitation</td>
</tr>
<tr>
<td></td>
<td>Including government and market regulation</td>
<td>Barriers to imitation</td>
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<tr>
<td></td>
<td>Stakeholders’ power to reduce costs</td>
<td>Barriers to imitation</td>
</tr>
<tr>
<td></td>
<td>Stakeholders’ power to increase revenue</td>
<td>Barriers to imitation</td>
</tr>
</tbody>
</table>

Sources: Adapted from: Post & Carroll (2006).
Stakeholder engagement helps mobilize multiple stakeholder interests, enhancing social capital. Social capital connects people or groups of people in social networks that generate solidarity, goodwill, and mutual influence, ultimately contributing to sustainable businesses and the common good (Maak, 2007). While there is widespread agreement that stakeholder engagement creates social capital, there is not an accepted measurement of the value of social capital.

<table>
<thead>
<tr>
<th>STAKEHOLDER GROUP</th>
<th>CONTRIBUTIONS</th>
</tr>
</thead>
<tbody>
<tr>
<td>Investors and lenders</td>
<td>Financial market recognition (reducing borrowing costs)</td>
</tr>
<tr>
<td></td>
<td>Capital equity and/or debt</td>
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<tr>
<td>Employees</td>
<td>Development of human capital</td>
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<tr>
<td></td>
<td>Collaborative workplace relations</td>
</tr>
<tr>
<td>Governments</td>
<td>Regulatory authorities</td>
</tr>
<tr>
<td></td>
<td>Macroeconomic and social policies</td>
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<tr>
<td>Local communities</td>
<td>License to operate</td>
</tr>
<tr>
<td></td>
<td>Mutual support and accommodation</td>
</tr>
<tr>
<td>Strategic resources and capabilities</td>
<td>Joint venture partners</td>
</tr>
<tr>
<td></td>
<td>Collaborative design, development, and problem solving</td>
</tr>
<tr>
<td></td>
<td>Reduce/reduce process and methodologies</td>
</tr>
<tr>
<td>Customers/owners</td>
<td>Supply chain</td>
</tr>
<tr>
<td></td>
<td>Enhance loyalty and reputation</td>
</tr>
<tr>
<td>Suppliers</td>
<td>Demand for and reputation</td>
</tr>
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</tr>
<tr>
<td></td>
<td>Reduce/reduce processes and methodologies</td>
</tr>
<tr>
<td></td>
<td>Network and value chain efficiencies</td>
</tr>
<tr>
<td>Workforce stability and conflict resolution</td>
<td>�</td>
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<tr>
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Westpac, an Australian bank, and Anglo American, a mining conglomerate, are two companies that have attempted to understand and explain how they benefit from better relations with stakeholders and increased social capital. Many companies find that strengthening societal relationships directly helps business operations. Healthy societies are more likely to support strong economies with thriving companies.

Graphic 2: How Valuing Community Stakeholders Benefits an Australian Bank

Source: Adapted from Westpac 2006 Stakeholder Impact Report, pg 51
Reducing Risk

Businesses can reduce financial, reputational, and political risks by engaging with stakeholders. This may be particularly true of companies with highly visible, prominent brands, which can be more understandable to regulatory changes. Stakeholder engagement helps companies understand the concerns and interests of employees, customers, NGOs, politicians and business partners. It also allows the company to see how fringe stakeholders use technology to meet their needs, and to provide a platform for better understanding of how to improve services and products to meet changing consumer needs. It may also be a way to identify new opportunities for innovation. Where there is risk, there is also opportunity. Because stakeholder engagement gives companies a better understanding of the society in which they operate, it can provide a platform for better understanding of how to improve services and products to meet changing consumer needs. Tapping Opportunities for Innovation.

“Overall, one cannot have a healthy economy and healthy and sustainable businesses in a fractured society.”
—Sir Mark Moody-Stuart, Chairman, Anglo American

Reducing Risk

Stakeholder Engagement and the Board: Integrating Best Governance Practices
Before privatization, piped water reached only about 60 percent of the households in the Philippines' capital city, Manila. Even worse, the public water utility lost about two thirds of the water in its system to leaks and unauthorized connections, which contributed to pressure and service problems for paying customers.

When Manila Water Company won the concession for water and wastewater services for the eastern half of Manila, it launched a "Walk the Line" in which all company staff visited customers. Consultations included residents of informal settlements ("IC, May 2007). Stakeholder engagement and cooperation was integral to improving service across the utility's service territory.

Stakeholder engagement and cooperation was integral to improving service across the utility's service territory. By working with and helping to organize resident cooperatives, Manila Water was able to install "mother meters" serving an entire community. The whole community is now held accountable for water consumption, and individual families pay community representatives.

Companies can become inward looking when directives are too closely aligned with management. Failure.

Engaging stakeholders in strategic conversations, management runs the risk of developing a very management-centric, inward looking view of the company’s capabilities and potential.

Management failure.

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Stakeholder Engagement and the Board: Integrating Best Governance Practices

Bypassing business level management and allowing information to flow between top management and outside stakeholders is an asset in a crisis situation. Effective stakeholder engagement reduces the possibility of a reputational crisis, and builds trust and understanding through deferring mutually understood values that address their respective interests.

Table 3: Continuum of Stakeholder Engagement

<table>
<thead>
<tr>
<th>Degree of Engagement</th>
<th>Management Behavior</th>
</tr>
</thead>
<tbody>
<tr>
<td>Reactive</td>
<td>Management only engages defensively when forced to.</td>
</tr>
<tr>
<td>Interactive</td>
<td>Management attempts to anticipate stakeholder concerns.</td>
</tr>
<tr>
<td>Proactive</td>
<td>Management has ongoing relationships of mutual respect.</td>
</tr>
<tr>
<td>Interactive</td>
<td>Company has ongoing relationships of mutual respect.</td>
</tr>
</tbody>
</table>

Source: Adapted from Hemphill (2006)
In August 1999, the Italian oil tanker “Laura D’Amato” was discharging its crude oil at Shell’s Gore Bay Terminal in Sydney, Australia. An oil spill of 300 tonnes of crude oil was spilled into the harbor, threatening the environment and nearby communities. The spill seriously threatened Shell’s reputation and business. The crisis could ruin stakeholder relations and encourage the government to stop commercial shipping in Sydney Harbour. A halt on shipping would directly affect Shell’s Gore Bay Terminal, which supplies 50% of New South Wales’ fuel requirements.

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The response:

Media:
Shell held a press conference at the site only three hours after the spill. A series of six media releases followed over the next two days. The response was widely distributed shortly after the spill was first discovered. The first media release was widely distributed shortly after the spill was first discovered.

The crisis developed. Background information sheets on Gore Bay Terminal and Sydney Harbour were distributed to all media. Shell spokespeople were available to speak to the media.

The key message was that Shell was taking immediate action to contain and clean up the spill. The company was working closely with the government and local residents to ensure the safety of the environment and the community.

The response strategy included:

1. Immediate action to contain and clean up the spill.
2. Communication with the public, media, and local residents.
3. Regular updates on the spill’s progress.
4. Engagement with stakeholders to address concerns.

The crisis management plan was activated, and Shell worked closely with the government and local residents to ensure the safety of the environment and the community.

The crisis was managed effectively, and Shell’s reputation was maintained. The company’s commitment to environmental responsibility was highlighted, and stakeholders were reassured that Shell was taking action to prevent future incidents.

The outcome:

Shell turned the crisis situation into a stakeholder relations victory. The company’s response was praised for its efficiency and effectiveness, and stakeholders’ concerns were addressed promptly. The crisis management plan was implemented, and Shell continued to work closely with local residents and government officials to ensure the safety of the environment.

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Government — Shell staff contacted senior advisers for the relevant ministers and
proactively offered for radio and television interviews, media briefings, one-to-one

Shell's rapid and comprehensive response to the crisis has resulted in a three-fold increase in strengthened public relations web activity, with a 300 percent increase in hits on the media releases web page in August compared to the normal monthly average.

The result:

Shell’s rapid and comprehensive response to the crisis has had reputational as well as tangible business benefits. Shell received widespread praise in crisis communications. There was no discernible impact on sales during the crisis, long-term business damage was avoided and Shell’s reputation with stakeholders was actually enhanced.

Shell turns crisis situation into a stakeholder relations victory (continued)
Support from the local community was immense. Many residents and local groups openly praised Shell’s involvement and relationship with them. After the crisis, Shell recorded higher than average attendance at the community consultation committee meetings and the next Gore Bay Terminal open day. During and after the crisis, the NSW Premier Bob Carr announced that Sydney is a working harbor that allows commercial shipping traffic. He ruled out closing Sydney Harbor either permanently or temporarily and said moving Gore Bay Terminal was not an option. Today, Gore Bay Terminal is still operational.

Source: Adapted from case study by Helen Morgner, External Affairs Officer, Shell Australia Limited.
Local priorities, such as livelihoods and cultural heritage, are not always shared by conservationists. Consequently, stakeholder engagement and constant communication is needed to reconcile differences. Early on, Rio Tinto set out to learn about the local cultural and economic environment to try to determine how the project could be integrated into the local society.

Since Rio Tinto plans to operate the mine in Madagascar through its QMM subsidiary for at least 40 years, it developed a community relations strategy based on mutual respect, active and reciprocal relationships, and a long-term perspective focused on mutual gains. QMM’s subsidiary, Q1, has been developed with the support of the Malagasy government. Q1 is committed to operating in a sustainable and responsible manner, respecting the local environment and the rights of local communities.

The company’s interest in integrating the mine with the local community is demonstrated by a special co-management agreement for renewable resources. After months of public consultation, the agreement was signed in 2002. The agreement involves the local population in the sustainable management of their renewable natural resources, and is reinforced by a DINA, a uniquely Malagasy social contract traditionally entered into in Madagascar to manage natural resources. More importantly, as they are anchored in custom and tradition, they render legal agreements culturally acceptable.

To make sure that the mine has a positive impact on Madagascar, beyond direct employment and tax revenue, Rio Tinto is sponsoring project enterprise and microfinance programs to support the development of local SMEs, and considering ways to build the capacity of local communal and government groups.

Ways to build the capacity of local communal and government groups.

**ENGAGING WITH CONSERVATIONISTS AND COMMUNITIES AFFECTED BY MINING (CONTINUED)**

"It is through consultation with affected communities that we are able to understand and monitor the effects of our operations. What is important is that those in affected communities have a reliable mechanism for bringing issues of concern and interest to our attention."

www.riotinto.com
The company has also partnered with environmental groups to manage the impact of the mine. In 2004, Rio Tinto developed a biodiversity strategy in consultation with experts from conservation and community development organizations, including the company’s biodiversity partners. In 2005, the partners and other organizations continued to assist Rio Tinto to develop a plan to implement the strategy. It commits Rio Tinto to have a net positive impact on biodiversity, wherever the company works.

For Rio Tinto, globalization spells opportunity combined with the need to engage better with the communities within which we operate. We recognize the importance of listening to, understanding and respecting the beliefs of those who do not understand or share our views. That takes time and resources, but it is worth the effort. Done well, it reduces risk and allows us to trade with and develop projects in nations that, not so long ago, opposed foreign investment and free trade.

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IV. BEST PRACTICES FOR PROACTIVE AND EFFECTIVE STAKEHOLDER ENGAGEMENT

There is no single engagement strategy that will work for all companies. Different types of businesses or operations will have different impacts and will therefore require different types of relationships or engagements with stakeholders. A nuclear power plant will, of course, need to have more substantial interaction with regulators and stakeholders than a bakery, and producers of highly visible name-brand products may need to do more engagement than producers of intermediate products.

This chapter includes an overview of how management should engage with stakeholders on a day-to-day basis. In addition to championing engagement as a core business value and ensuring that management is engaged in ways that satisfy and exceed stakeholders’ expectations, managers should strive to build trust and mutual respect.

General guidelines for management best practice:

- Start early. Relationships take time to build. Trust and mutual respect are established over time. Trust is also much harder to build if stakeholders are only consulted when there is a problem or crisis.
- Keep an open mind. The outcome of a truly open and responsive engagement process cannot be defined in advance as solutions that satisfy multiple parties can seldom be guessed at beforehand. Consultation where the company has already determined their plan of action is likely to be perceived as an untrustworthy public relations exercise.
- Manage engagement as a business function. Taking a systematic approach that is grounded in the business strategy and operations increases the likelihood that engagement will create value.
- Tailor engagement practices to the needs and interests of the company and its stakeholders. Explain what input is needed from stakeholders and how it will be used in the decision-making process — again, during the “shared values” continuum.
- Manage relationships. Build and maintain relationships that last.
- Keep in mind. The outcome of a truly open and responsive engagement process cannot be defined in advance as solutions that satisfy multiple parties can seldom be guessed at beforehand. Consultation where the company has already determined their plan of action is likely to be perceived as an untrustworthy public relations exercise.

In addition to championing engagement as a core business value and ensuring that management is engaged in ways that satisfy and exceed stakeholders’ expectations, managers should strive to build trust and mutual respect.
Take a long-term view. For issues that are intrinsically related to company

Identifying and Prioritizing Stakeholders and Their Issues

*Take a long-term view. For issues that are intrinsically related to company*

Engaging with Stakeholders:
The following are useful questions to consider when determining how to begin:

1. Who are our stakeholders?
2. Which groups are voluntary stakeholders (e.g., employees and shareholders)?
3. What do we think their interests are?
4. What opportunities and challenges do they present?
5. What responsibilities and obligations (economic, legal, ethical, and philanthropic) do we have to different stakeholders groups?

Strategically, in a way that will be useful for a company:
Engaging stakeholders:

Because it is neither possible nor desirable to engage with every possible stakeholder on every conceivable issue, appropriate planning is necessary to engage strategically, in a way that will be useful for a company.

Businesses generally begin engaging with core stakeholders, those that have the most legitimate and urgent issues or those most likely to have an obvious, direct impact on the business. Another way of deciding where to begin is looking at the issues of those most likely to have the most significant and urgent issues or those most likely to have the most significant and urgent issues.

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6. What strategies, actions, or decisions should we take to best deal with these responsibilities?

Stakeholders will also decide what issues matter and they will do this regardless of how company managers prioritize issues. It is essential for management to be open to stakeholder concerns to understand what they are and to be able to respond to new concerns when that is appropriate.

Stakeholder mapping involves creating a visual diagram to help analyze and prioritize stakeholder groups. The graphics below provide an example of a template.

Another way to prioritize stakeholders is to take a list of all stakeholders and rank them based on their influence or importance to the company. For engagement to be perceived as credible, it should be as open and transparent as possible. Even shareowners can have very different opinions and interests, and their concerns may differ from other stakeholders.

Stakeholder mapping involves creating a visual diagram to help analyze and prioritize stakeholder groups. The graphics below provide an example of a template.

New concerns will also arise, and we must be able to respond to them. All stakeholders have a right to be heard, and it is essential for management to be open to shareowner priorities. It is essential for management to be open to stakeholder concerns to understand what they are and to be able to respond to them.
Graphic 3: Prioritizing Stakeholders - Royal Dutch Shell

Graphic 4: Prioritizing Stakeholders - Template
Table 4: Prioritizing Stakeholder Groups

<table>
<thead>
<tr>
<th>STAKEHOLDERS</th>
<th>DOES THIS GROUP STRONGLY INFLUENCE THE COMPANY'S PERFORMANCE?</th>
<th>IS THIS GROUP STRONGLY INFLUENCED BY THE COMPANY'S PERFORMANCE?</th>
<th>WILL THIS GROUP STRONGLY INFLUENCE OR BE STRONGLY INFLUENCED IN THE FUTURE?</th>
<th>TOTAL</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>ECONOMIC</td>
<td>ENVIRONMENTAL</td>
<td>SOCIAL</td>
<td>ECONOMIC</td>
</tr>
<tr>
<td>EMPLOYEES</td>
<td>1</td>
<td>0</td>
<td>1</td>
<td>1</td>
</tr>
<tr>
<td>CUSTOMERS</td>
<td>1</td>
<td>1</td>
<td>1</td>
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<tr>
<td>LOCAL COMMUNITY</td>
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<td></td>
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<tr>
<td>INVESTORS</td>
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<tr>
<td>SUPPLY CHAIN</td>
<td></td>
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</tbody>
</table>

Deciding Which Issues are Material to Stakeholder Engagement

In accounting, information is considered material if its omission or misstatement could influence the economic decision of users taken on the basis of financial statements. For the purposes of stakeholder engagement, material information is anything that, if unknown or misunderstood, would prohibit management or stakeholders from making sound judgments and taking appropriate action.

One tool for helping to define the materiality of issues is AccountAbility’s five part materiality test. To help with engagement planning, this test can be used to rank issues as being of high, medium, or low materiality in the following five areas:

- Of course, a company may underestimate the importance of a particular issue to a key stakeholder group. Materiality rankings give some indications about where to begin an engagement process, but the goal is to be transparent and open in an engagement. Hence, the company must be sensitive to the ways it identifies and discusses issues.
- Issues that are considered social norms.
- Issues that are considered important enough to act on (now or in the future).
- Issues that the company’s stakeholders consider important enough to act on.
- Issues where the company faces agreed policy statements or strategic issues.
- Issues that have direct short-term financial impacts.

One tool for helping to define the materiality of issues is AccountAbility’s five part materiality test. For the purposes of stakeholder engagement, material information could influence the economic decision of users taken on the basis of financial statements. For the purposes of stakeholder engagement, material information could influence the economic decision of users taken on the basis of financial statements. For the purposes of stakeholder engagement, material information could influence the economic decision of users taken on the basis of financial statements.
Stakeholder Engagement and the Board: Integrating Best Governance Practices

Regulators, investors, consumers, competitors, and suppliers. For stakeholders that are most closely linked or impacted by a company, face-to-face meetings are most appropriate. Open houses, public forums, and disclosure may suit the needs of other stakeholder groups.

While ad hoc stakeholder engagement is generally less valuable than ongoing processes, stakeholders may attach to the issue.

Different types of stakeholders will have different preferences for how they prefer to interact with a company. It can be helpful to ask stakeholders how they wish to engage with a company and what their expectations are for the interaction. Each stakeholder group is unique and may have different communication needs or concerns.

Formal engagement can take many forms, from partnerships with NGOs, to formal community engagement programs or advisory bodies. Local communities impacted by mining or oil drilling can serve as representatives or local communities affected by extractive industries projects. Where a company has a formal advisory council or Community Consultative Council, which is comprised of representatives from diverse stakeholder groups, it may be helpful to develop ongoing forums to facilitate communication and address concerns.

For example, a financial services company uses a standing advisory body to address concerns. The company’s chief executive officer annually convenes a Community Consultative Council, which is comprised of representatives from 20 diverse stakeholder groups. Each participant is invited to highlight emerging concerns or trends and to discuss how the bank should address them and how much relevance stakeholders give to each issue. Advisory bodies can serve as a more robust conversation, where a company solicits input from and learns from stakeholders. Forward engagement can take many forms, and find appropriate representatives of stakeholder groups with which to engage.

Dialogue is a more robust conversation than consultation, which is a one-way flow of information, where a company solicits input from stakeholders. Dialogue allows stakeholders to share their perspectives and concerns and to engage in a meaningful discussion. Engagement is generally less valuable than ongoing processes, but can be useful in the early stages of engagement when stakeholders are first introduced to a company and its initiatives. Stakeholders that are most closely linked or impacted by a company’s projects and operations are most likely to have ongoing relationships with the company and to be familiar with its products and services. For stakeholders that are impacted by a company’s projects and operations, open houses, public forums, and disclosure may be more effective than ongoing processes.
The table below lists all of the ways that Anglo American engaged with various stakeholders during 2006.

**Table 5: Channels Anglo American Uses to Engage with Different Stakeholder Groups**

<table>
<thead>
<tr>
<th>External Stakeholders</th>
<th>Key Channels for Engagement in 2006</th>
</tr>
</thead>
<tbody>
<tr>
<td>Investors</td>
<td>Results presentations, road shows, annual presentations, sustainable development presentations, involvement in partnerships, quarterly presentations, Human Rights, etc.</td>
</tr>
<tr>
<td>Governments</td>
<td>Direct engagement and through industry associations, national assessments, partnership with the World Bank and UN Principle on Business and Human Rights, engagement with the Global Business Coalition on HIV/AIDS, etc.</td>
</tr>
<tr>
<td>International</td>
<td>Membership of UN Global Compact, IoM, WBCSD and EITI, Voluntary Assessment on Human Rights, etc.</td>
</tr>
<tr>
<td>Contractors and</td>
<td>Open days, safety inductions, commercial interactions, tender and compliance processes, human rights partnerships, social investment partnerships, etc.</td>
</tr>
<tr>
<td>Suppliers</td>
<td>Commercial relationships, complaints procedures, surveys</td>
</tr>
<tr>
<td>Customers</td>
<td>Commercial relationships, complaints procedures, surveys</td>
</tr>
<tr>
<td>NGOs</td>
<td>Commercial relationships, complaints procedures, surveys</td>
</tr>
</tbody>
</table>

*Source: [http://www.angloamerican.co.uk/static/reports/2007/sc-engagement.htm](http://www.angloamerican.co.uk/static/reports/2007/sc-engagement.htm)*)
Developing a Structure for Success

Once stakeholder groups and issues are prioritized and engagement methods are considered, the process of developing relationships with stakeholder groups can begin. At the outset, the agenda for engagement should be discussed, so that goals and expectations are mutually agreed in advance. Most engagements can begin at the outset; the agenda for engagement should be discussed, so stakeholders are consulted. The process of developing relationships with stakeholder groups is essential. The importance of communicating consistently is emphasized. Someone should be designated as the primary contact for the project or relationship.

Using Information from Stakeholder Engagement

Stakeholder engagement provides valuable information that could produce a shift in company thinking or practice. Other stakeholder concerns can be addressed relatively easily. A stakeholder engagement process for the Angola Liquefied Natural Gas project, a multibillion dollar venture located in Soyo on Angola’s northwest coast, relied heavily. A stakeholder engagement process for the Angola Liquefied Natural Gas project was funded. Other stakeholder concerns can be addressed relatively easily. A stakeholder engagement process for the Angola Liquefied Natural Gas project was funded.

It is essential that all employees are clear about the processes, objectives and commitments they are executing. Some employees also need to consider the importance of communicating consistently.

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coast, uncovered villagers' concerns about protecting their homes from venomous snakes and other dangerous reptiles displaced during clearance of the construction site. To address this concern, the energy companies involved in the project hired a herpetologist to capture the reptiles and relocate them to remote areas under the authority of local environmental regulators.

Increasingly, businesses are moving from informing and responding to involving stakeholders directly in projects. In Morocco, Lafarge Cement involved community members in the process of finding a new location for a cement plant. While the company generally attempts to reduce impact on the environment and demonstrate benefits to the local economy, the public often views cement plants as noisy and destroying landscapes. Lafarge decided to build a new factory, which was initially planned to be located right in the middle of the town. After several rounds of discussion, the new plant was moved to a new location, away from the town center. Lafarge conducted public meetings to involve residents in the decision-making process, which resulted in universal acceptance of the new plan.

How does a company determine which stakeholder interests and concerns it should address? A company must meet its economic responsibilities (being profitable) and its legal responsibilities (being in compliance with government regulations and laws). Stakeholder interests that conflict with these responsibilities cannot be addressed.

Increasingly, businesses are moving from informing and responding to involving stakeholders directly in projects. The number of serious issues in involving and responding to stakeholders directly in projects. The company publicly reports on its performance in reducing the number of serious issues in involving and responding to stakeholders directly in projects.

During the process of engaging stakeholders, issues and concerns will come up that a company may not be able to address. Stakeholders often ask pharmaceutical companies to reduce or eliminate their use of animal testing, but many governments require animal tests for product approval. Some pharmaceutical companies, such as GlaxoSmithKline, note that they disagree with stakeholders on this issue. Novo Nordisk, the world's largest maker of insulin products for diabetics, acknowledges that reducing its reliance on animal testing is desirable, but it can only do so when governments change their approval processes for products. Novo Nordisk recently reported on the number of animals used in testing and the company's success in changing government policies.
reasonable, however, about receiving stakeholder engagement responses. Addressing stakeholder concerns may involve additional costs, such as the hiring of specially trained experts to manage removal of snakes at the Angola LNG project. However, over the long run, these costs may be offset in other ways, such as ease of project expansion or reduced site vandalism, or even avoidance of product sabotage by disgruntled employees drawn from the affected community.

A company should also look to the long-term implications of projects that respond to immediate stakeholder concerns and may need to be broader in scope or require a different strategy to be fair to other stakeholders. For instance, Anglo American's early efforts to provide antiretroviral drugs to employees with HIV/AIDS soon revealed that the initiative had limited impact unless family members were also treated. Similarly, building schools and communities around large resource extraction projects can create dependency on the part of communities with a negative impact when the business shifts from operations, downsizes, or moves to a different location. Mining companies frequently find that investing in the immediate community can create jealousy from neighboring communities and lack of capacity among local authorities to manage the royalties from mining operations (see commdev.org).

Communication with Stakeholders

Follow-through is important to any relationship and this certainly applies to relationships with stakeholders. Whether or not a company is able to implement what it has learned from stakeholders, there is an obligation to report back, to make it clear that stakeholder concerns and interests were heard, considered, and valued in addition to reporting back to specific stakeholder groups. Sustainable reporting provides companies with an opportunity to make it clear that stakeholder concerns and interests were heard, considered, and valued, in addition to reporting back to specific stakeholder groups. Stakeholder engagement is reasonably be pursued in the short term, long-term plans, such as working to
Companies have a responsibility to respond to stakeholders about concerns shared, to explain how or whether concerns or suggestions are being addressed. In addition to responding to issues raised by stakeholders, companies should keep track of any promises or commitments they have made. Just as a company would hold themselves accountable for promising earnings growth to shareholders, commitments to community members or NGOs need to be taken seriously. Companies should respond to stakeholders about concerns shared. To explain how or whether concerns or suggestions are being addressed, companies should report on commitments made.

COMMUNICATING LOCALLY: USING STREET THEATRE IN INDIA TO HELP CHILD LABORERS

To address the problem of child labor, Bayer CropScience established creative learning centers in rural India to prepare child laborers for state-run schools and used street theater — called kala jatha — to communicate the need for school education to local residents. When Bayer CropScience acquired an Indian seed company, ProAgro, in 2002, it was concerned about the large number of children working on their hybrid cotton fields in Andhra Pradesh, India. NGOs found hundreds of children working for different multinational companies and considered a supply chain problem. Children in rural India do not perceive child labor as a threat. Bayer CropScience partnered with an NGO to establish creative learning centers in rural India to prepare child laborers for state-run schools and use street theater to communicate the need for school education to local residents.
The company pays a bonus ranging from 5 to 7.5 percent of the purchase price of seeds. At the same time, violations of the ban are met with graduated penalties.

To be valuable, multi-stakeholder reports should be characterized by candor, social, environmental and economic impacts and performance. Annual sustainability reports are one of the ways that a growing number of organizations around the world are communicating with stakeholders about their performance in a process for monitoring internal performance improvements. A sustainability reporting process is aimed at a wide, multi-stakeholder audience. It is a tool to report performance on issues that stakeholders care about, as well as a process for communicating with stakeholders on the outcome of consultations or dialogues.

NGOs have been invited to participate in field checks to verify and confirm significant declines in child labor. As part of the company’s reporting process, the performance in rural villages has been reported on in the sustainability report. Bayer has also reported on these initiatives in child labor. Bayer and Naandi sponsored street theatre performances of the need for school education. Bayer and Naandi sponsored a theater troupe to perform in the local villages. To increase awareness among cotton farmers, Bayer contributed to a campaign to promote children to join school. The company launched a network of creative learning centers throughout Andhra Pradesh. The company has successfully prepared children to join school. To provide opportunities for child laborers, Bayer partnered with an Indian-based NGO, Naandi, to launch a network of creative learning centers throughout Andhra Pradesh.

To be valuable, multi-stakeholder reports should be characterized by candor, social, environmental and economic impacts and performance.
stakeholder groups — who they are and their main needs and positions — as well as a description of stakeholder engagement processes and a summary of how the company is responding to and addressing stakeholder priorities. In addition, evidence of how feedback and engagement processes have been integrated into the company’s decision-making processes, supported with examples of results from this integration.

An increasing number of sustainability reports now make use of independent third party assurance services, such as shareholder panels, subject matter experts, and professional assurance providers, to play an increasing role in enhancing the credibility of sustainability reporting.

**The value of best practice**

The value of best practice sustainability reporting is that it requires an organization to view sustainability issues not just in terms of producing a report but in terms of managing sustainability issues not just in terms of an organization to view sustainability reporting as that it and what it is doing to respond to the issues of stakeholder needs and concerns — including consideration of third party assurance to assist in the organization and data in the report are reliable and based on sound information and management systems. Sustainability from this perspective, the company’s decision-making processes, supported with examples of results of how feedback and engagement processes have been integrated into the company’s decision-making and addressing shareholder priorities. In addition, a description of shareholder engagement processes and a summary of how shareholder groups — who they are and their main needs and positions — as well as...
Several international standards have evolved which serve as useful guides for companies on how to engage with stakeholders in a responsible and accountable manner. These include the following:

- **AA1000**
  - Published by The Institute of Social and Ethical Accountability (or AccountAbility), the AA1000 Series is a set of principles-based standards designed to guide companies in implementing systems to improve their sustainability performance and engagement with stakeholders.
  - The AA1000 Series was released in 2008 following extensive stakeholder consultation and is built on a key foundation principle of inclusivity, which is defined as “the participation of stakeholders in developing and achieving an accountable and strategic response to sustainability.”
  - To meet the AA1000 Standard, companies must demonstrate an accountable and strategic response to sustainability.

![Evolution of Sustainability Reporting](source: Global Corporate Governance Forum Presentation)

The following sources are recommended for company communications to stakeholders needs:

- Public Relations
- Response to Stakeholders
- Meeting Disclosure Requirements
- Integration into Business Processes

Graphic 5: Evolution of Sustainability Reporting

Source: Global Corporate Governance Forum Presentation
Stakeholder Engagement and the Board: Integrating Best Governance Practices

The tool assesses how well a company’s disclosure enables readers to draw informed and thoughtful conclusions about the company’s performance.

A benchmarking tool to assess sustainability reports was introduced by SustainAbility.

www.accountability.org.uk

GRI Guidelines

The Global Reporting Initiative Sustainability Reporting Framework is the most widely used and globally recognized framework for sustainability reporting. It comprises a set of core principles to guide companies in selecting and compiling material information on material issues, including social, environmental, and economic aspects of their operations. It also includes a set of standard corporate disclosures and specific performance indicators that are relevant to various industries and serve as benchmarks for reporting.

www.globalreporting.org

OECD Guidelines for Multinational Enterprises

Organizes consultation and cooperation between employers and employees, and provides a set of core principles to guide companies in selecting and compiling material information on material issues, including social, environmental, and economic aspects of their operations. It also includes a set of standard corporate disclosures and specific performance indicators that are relevant to various industries and serve as benchmarks for reporting.

www.oecd.org

SustainAbility

A benchmarking tool to assess sustainability reports was introduced by international think-tank, SustainAbility, in its 2000 report, “The Global Reporters.” The tool assesses how well a company’s disclosure enables readers to draw informed and thoughtful conclusions about the company’s performance.

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www.sustainability.com/insight/globalreporters.asp?id=458

Conclusion

The tool assesses how well a company’s disclosure enables readers to draw informed and thoughtful conclusions about the company’s performance.

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Access to the necessary competences and resources to operate the process of stakeholder participation:

A process of ongoing stakeholder participation that is integrated and applied

An explicit commitment to be accountable to stakeholders

www.sustainabiliy.org.uk

Stakeholder Participation

Across the organization, both at group and local level

Across the organization, both at group and local level

A process of ongoing stakeholder participation that is integrated and applied

An explicit commitment to be accountable to stakeholders
Stakeholder Engagement and the Board: Integrating Best Governance Practices

The UN Global Compact is the largest corporate citizenship and sustainability initiative in the world. More than 5,000 corporations from 130-plus countries have committed to support and respect 10 universally accepted principles in the areas of human rights, labor, the environment, and anti-corruption. Signatories are also required to report on their performance against the 10 principles.

Because stakeholder engagement is a part of responsible, ethical management, board members should be briefed about engagement practices and outcomes. Just as the board should be involved in financial reporting, at least a portion of the board should be involved in nonfinancial management. Board members should be briefed about stakeholder engagement outcomes that address and respond in an accountable way to issues and impacts in strategies, plans, actions, and results in comprehensive and balanced reports. Stakeholder engagement processes should ensure that all stakeholders are engaged and that the organization responds in a responsible and accountable manner.

Inclusion requires a defined process of engagement and participation that provides clarity about responsibilities. A stakeholder engagement process is intended to support and respect human rights, the environment, and anti-corruption.

The UN Global Compact is the largest initiative in the world. More than 5,000 corporations have committed to support and respect the 10 principles. Stakeholder engagement processes should ensure that all stakeholders are engaged and that the organization responds in a responsible and accountable manner.

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In some companies, nonfinancial or sustainability reporting is overseen by the audit committee. There are also boards with committees dedicated to corporate responsibility or sustainability that monitor or oversee stakeholder engagement and sustainability reporting.

For stakeholder engagement to lead to a meaningful extension of corporate accountability, there needs to be some mechanism by which stakeholder views can feed directly into corporate decision-making and by which stakeholders can hold management to account. In most instances, stakeholders are not represented on company boards. An advisory body can provide representation for stakeholders through a second tier within the governance structure [Owen et al., 2001].

As part of the nonfinancial reporting process, more and more companies are having stakeholder groups review and comment on the company’s approach to assessing and reporting on social and environmental performance related to corporate activities. This can take the form of an independent advisory committee or stakeholder panel to serve as proxy for stakeholder groups.

Particularly for companies without shareholder representation in the boardroom, some mechanism is needed to ensure stakeholder views feed directly into corporate decision-making. Having a non-executive director involved in or as chair of the group can further ensure that recommendations are shared with the board, allowing the board to take a direct interest in these issues and the way they might inform key decisions. Importantly, the advisory board should be given direct access to the board to ensure that the board gets a broad sense of outside perspectives of the company.

Best Practices for Stakeholders

Cooperation has grown out of efforts to tackle complex environmental problems. While there are still plenty of instances of antagonistic relationships between stakeholders and businesses — including industrial espionage and product recalls — there is growing recognition of the value of collaborative, stakeholder-focused strategies.

Collaboration has grown out of efforts to tackle complex environmental problems. Much of the development in broader stakeholder collaborative problem-solving has occurred in the context of the environmental movement, particularly in the area of environmental protection and product safety. While there are still plenty of instances of antagonistic relationships between stakeholders and businesses — including industrial espionage and product recalls — there is growing recognition of the value of collaborative, stakeholder-focused strategies.

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Various partnerships have emerged across the globe during the past 15 years to address problems such as packaging, deforestation, and mining.

Looking Forward: Emerging Trends in Stakeholder Engagement

In the interest of shareholders and other stakeholders, working conditions may create a more committed, productive workforce which is more agile for consumers and shareholders in the long-term, providing better social impact for shareholders. In some cases, this may require looking at long-term versus short-term trade-offs in addressing the interests of shareholders. In some cases, it may mean working more closely with employees, who may represent significant costs to a business. Stakeholders can be most effective if they focus on areas that produce gains and address problems such as packaging, deforestation, and mining.

Understanding stakeholder needs, interests, and concerns is a fundamental part of social impact measures. Social investment indices, such as the Dow Jones Sustainability Index, give more weight to stakeholder engagement than to any other factor. For example, the index rates companies based on their performance on social, environmental, and governance criteria, which can be measured through stakeholder engagement. In response to new issues, such as climate change, companies have been driven by shareholder activism and increased awareness of the need for responsible business practices. The measurement of shareholder engagement used in standards, guidelines, and performance assessments such as the Dow Jones Sustainability Index is likely to increase in importance.

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Understanding stakeholder needs, interests, and concerns is a fundamental part of managing indirect or nonfinancial risks. In fact, nonfinancial risks often have their own associated costs—whether social, environmental, or economic—and will likely affect the company's financial bottom line. Engaging with stakeholders, and using information from stakeholder engagement in decision-making, is fundamental to understanding nonfinancial risks and managing them effectively. Stakeholder collaboration has also been impacted by the rise of globalization. In response to new issues, such as climate change, companies have been driven by shareholder activism and increased awareness of the need for responsible business practices.
Stakeholder Engagement and the Board: Integrating Best Governance Practices

In other words, companies are judged on whether they do or do not engage. More sophisticated measures of engagement are being developed to measure the degree of "embeddedness" of stakeholder engagement, and it is likely that scrutiny of engagement capabilities will increase.

At the same time, as society's expectations about private enterprise change, companies may need to engage on a broader number of issues. Increasingly, issues that are important to society—water scarcity, HIV treatment, and climate change—are becoming important issues for companies to address. Boards and executive leadership will need to be engaged in setting strategies and priorities, and to have ways to monitor the outcomes.

Finally, in a move toward corporate governance systems that are truly responsive and accountable to stakeholder interests, more and more companies are choosing to develop collaborative partnerships with stakeholder groups and to enlist stakeholders to propose solutions or monitor outcomes. To be effective and fair, these governance systems should also have the capacity to respond to differences in power and access to resources between and within stakeholder groups.

In "Plan B 3.0 — Mobilizing to Save Civilization," Lester Brown of the Earth Policy Institute makes the case that indirect costs associated with production of goods and provision of services have until now been left off the books. These costs, which are the real cost of oil or water versus the need to maintain and replenish water resources, or the cost of eliminating pollution or managing soil quality and not just production, or use of land or water, are not accounted for in the market when setting prices. For example, what is the real cost of carbon emissions? Or use of water versus the need to maintain and replenish water resources? Or the cost of ensuring oil security and not just production? Or use of land or water?

In the past, these costs have been borne by stakeholders outside the business. Now, these costs are expected to be internalized into the market price. But this is not yet happening. As governments adjust their economic policies to take these costs into account, a similar adjustment will be needed by businesses to fully account for these costs and impacts on various stakeholders — or their products and services. Conversely, boards and executives will need to be engaged by businesses to fully account for these costs and impacts on various stakeholders — or their products and services.

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Companies may need to engage on a broader number of issues, but it is likely that scrutiny of engagement capabilities will increase.
It is thus possible to envision a business world not characterized by the ongoing shareowner/stakeholder debate, but one where shared values are negotiated between the company and various stakeholders (including shareowners) by collaborating with stakeholders to solve complex and demanding social, health, safety and environmental problems. Companies should be able to create even more value for shareowners and benefit society at the same time.
USEFUL RESOURCES OF SELECTED ORGANIZATIONS AND INFORMATION SOURCES

Recommended Reading


Recommended Reading


Association of British Insurers, (2004), Risk, Rewards and Responsibility

Budapest Business Ethics Centre, Ethics and Trust in Economic Relationships

Ernst & Young South Africa, Governance and Sustainability, Tool for Directors

Financial Reporting

Risks


http://www.unglobalcompact.org/content/NewDocs/Whocareswinsｳегодня.pdf

http://www.unglobalcompact.org/content/NewDocs/Whocareswinsent.pdf

http://www.unglobalcompact.org/content/NewDocs/Whocareswins1.pdf

http://www.unglobalcompact.org/content/NewDocs/Whocareswins2.pdf


http://www.unglobalcompact.org/content/NewsDocs/WhoCaresWins.pdf
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The Oil, Gas and Mining Sustainable Community Development Fund (ComDev), Stakeholder Engagement help://comdev.org/consulting/consultant/consulting/Publications/GoodPractice-


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Stakeholder Engagement and the Board: Integrating Best Governance Practices

For Further Reading


Stakeholder Engagement and the Board: Integrating Best Governance Practices


Persuading Companies to Address Social Challenges. The Ford Foundation.


SustainAbility and UNEP. (2002). Trust Us: The Global Reporters 2002 Survey of


Transformations in Global Governance: Implications for Multinationals and Other Stakeholders. (pp. 120-145). Cheltenham, UK: Edward Elgar.

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