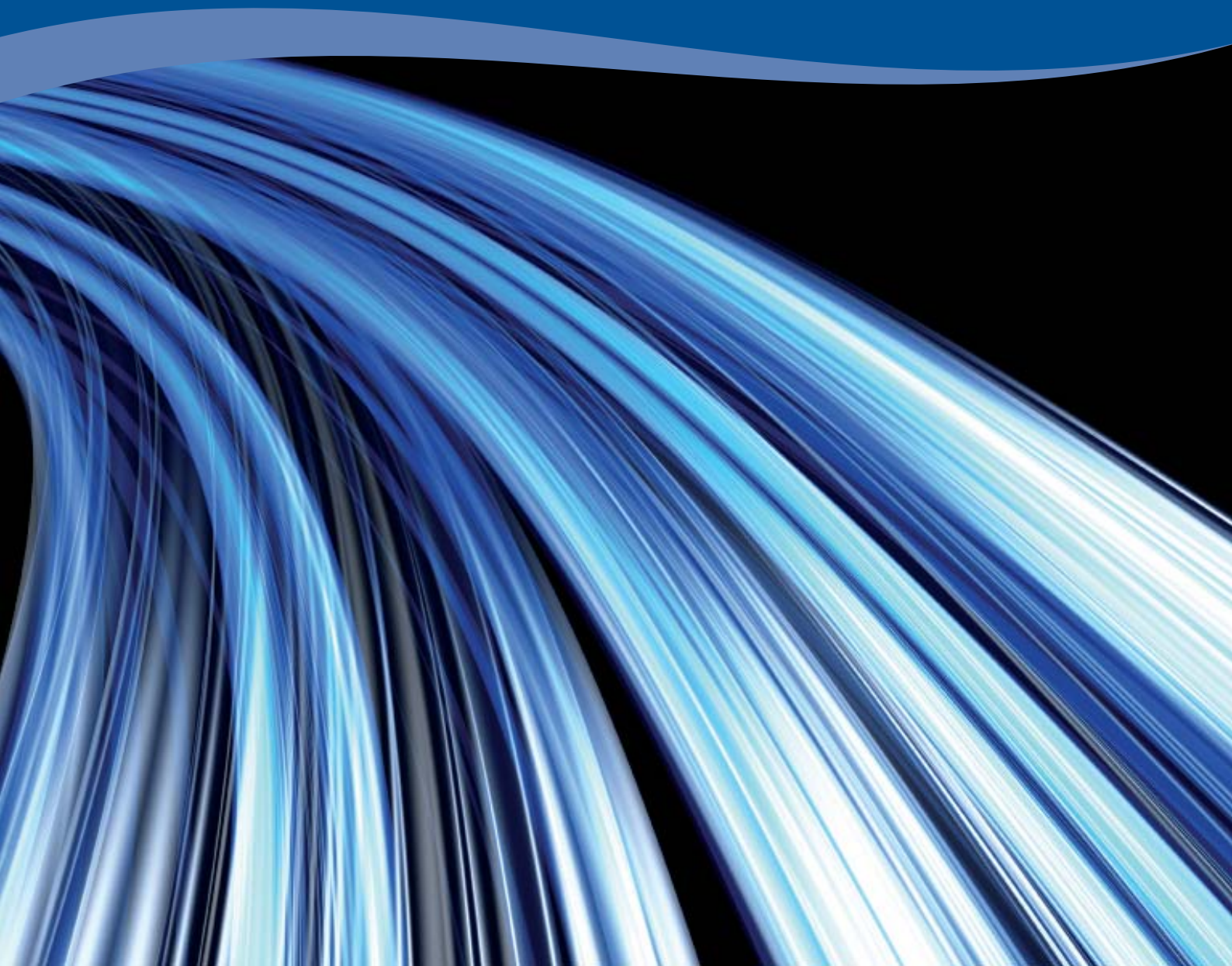


White Paper

Sustainability, responsibility and governance: the challenges of leading an organisation in complex times

Peter Davis



Lord Leverhulme once famously observed that he knew half of his advertising to be effective; he just didn't know which half. Many companies today feel much the same about their Corporate Responsibility (CR) and sustainability programmes: they know that some of it is necessary, but they are often rather hazy about which bits, and why.

This situation is not helped by the fact that CR and sustainability remain rather imprecise terms. For some companies CR remains synonymous with philanthropy, community projects and charitable donations. For others, the environmental – particularly the climate change – aspect of the sustainability agenda holds centre stage. For others again it includes more novel and complex issues such as human rights and business ethics.

At the moment things are further complicated by the worsening economic environment. Are CR and sustainability are 'bull market' phenomena that will wither as colder economic winds begin to blow?

The simple answer to that question is no, they are not. Certainly, much of the 'fluffier' philanthropic aspects of corporate practice will decline with the economic slow-down. However, proper CR and sustainability practice will continue and deepen for the simple reason that they are increasingly central to business success, or even survival.

The development of CR and sustainability reflect the reality that companies are having to operate in much more complex environments than was the case in the past, and are required to take account of factors which would historically not have been regarded as 'business issues'. These issues cannot be disregarded, as they have direct commercial and operational relevance, so cannot be ignored. CR and sustainability, properly undertaken, reflect the most important challenge facing managers today: how to manage complexity?

To talk about the need 'to manage complexity' may not seem anything new. An article in *Management Today* in April 2008 examined the issue of complexity. It assembled a group of business 'gurus' to solicit their opinions. For Mike Gibson of PwC, complexity emanates from the tensions between different legal structures around the world, and the problem of accountability in large organisations. According to WPP's Sir Martin Sorrell, complexity derives from "an increasingly networked world". BUPA's then-CEO, Val Gooding argued that increasing customer demands lies at the heart of complexity.

Of course, all these people are correct – business life has become more complex because of all the issues that they highlight.

However, at the same time, they have completely missed the point. Certainly, managing an organisation has become more complex because various elements of 'normal' business life have become more complex. However, the central reason why business has become more complicated is because leaders and managers now need to address entirely novel issues; issues to do with politics, society, ethics and the environment which historically were not seen as having anything to do with the private sector or with the management of a commercial organisation.

CR and sustainability are windows onto this complexity. Companies which realise the importance of these issues and which manage them well realise that there are new issues and new stakeholders which have

significant impacts on the business, and which therefore need to be managed as assiduously and effectively as more traditional operational considerations.

Complexity and these new issues can be broken down into three broad, overlapping categories:

Environment

The issues of global warming and climate change have been well-rehearsed, and given significant coverage. However, for many companies, the proverbial polar bear on an iceberg is not the problem. The problem are specific aspects of the environmental agenda which are beginning to have operational impacts on companies in their daily operations.

Environment and the construction sector

Many Victorian commercial and industrial buildings are still being used today. By comparison, the average life expectancy of a modern London office building is 17 years, from construction to demolition. This culture of 'disposable buildings' has been facilitated by relatively low cost of key building materials, and the availability of landfill. As a result, the construction sector has become very adept at specifying and constructing buildings that are 'light and tight'.

However, things are changing. The landfill levy is making construction waste increasingly expensive; many key building materials are increasing in price - a function in part of their scarcity; and occupiers are now demanding more energy-efficient buildings. As a result the property and construction sectors are having fundamentally to re-assess how they do business, and what constitutes 'value' in a building.

Mining – the impact of water

Smelting processes, for example of bauxite, are extremely water-intensive. Water has therefore always been an issue that mine managers have had to be aware of. However, the nature of this challenge is changing significantly. Historically, it was important for mining companies to ensure that the water they used in smelting was decontaminated, and returned to water courses in a decent state.

Now though, climate change is leading to water shortages in many more areas, particularly in parts of Africa. As a result, the challenge mining companies now face is one of gaining access to sufficient water, and doing so without denying local populations access to clean water. Responding to this challenge will mean research and investment into new technologies.

'Food miles'

Ever since it was proposed, the concept of food miles has provided the consumer with an apparently-simple short-hand for the distance travelled by the food products they buy. As a result, business practices that had become routine, such as importing out-of-season produce from places like Spain and Africa have come under considerable scrutiny.

However, it has now become clear that focussing on food-miles is not necessarily helpful in terms of understanding the 'carbon footprint' of a product. A 2005 Defra report indicated that it can be more energy-

efficient to import tomatoes from Spain by lorry than to grow them in a heated greenhouse in the UK. Lettuce grown out of season in the UK also compared unfavourably with Spanish salad when total carbon emissions were measured. Things become more complex still when one factors in the wider human impacts of current global trade patterns.

People

There is also an increasing expectation that companies take account of the impacts of their activities on the wider communities and people on whom their businesses impact.

Supply chains

Changing patterns of global trade in the past two decades mean that many companies now source goods from developing countries like India, China and Brazil. For many western retailers, shifting manufacturing to low cost countries seemed a no-lose way of increasing margins in a competitive market.

However, things have not proved so straight-forward. As many companies in the apparel sector have discovered: they are now held responsible for labour conditions and working practices in their supply chains. The most recent example emerged from a BBC Panorama programme. Their investigations had brought to light that items for sale in the Primark chain of shops were being hand-stitched by children in India. As they and many other companies have discovered: the fact that the factories at fault are contractors, rather than owned, is irrelevant: the high-street brand-owner is held responsible by the consumer for labour conditions in the supply chain.

Nor is it just apparel companies who need to deal with these issues. In 2007, toy-maker Mattel had to withdraw from sale several million faulty toys manufactured in China and Mexico. Food companies too are having to account for the pay rates and working conditions on plantations and in processing plants whence products like chocolate, coffee and tea are sourced.

Human rights

Protection of human rights seems like something with which governments, not businesses, should concern themselves. However in the past decade, companies have found themselves attacked for the human rights impacts of their operations. In 1996, Shell was accused of complicity in the execution by the Nigerian government of Ken Sara-Wiwa and other activists: a case against Shell will be heard in the courts in the US in early 2009. Canada's Talisman Oil was forced to sell its stake in the Greater Nile oil project in Sudan following claims by campaigners that the company had assisted the Sudanese authorities in their "brutal ethnic cleansing campaign" against southern separatists.

In responding to these new expectations, companies are undertaking activities very different from anything they may have done in the past. Statoil, for example worked with the Venezuelan government in its efforts to improve human rights practice in the country. The company funded an initiative to provide human rights training to judges. The programme

reached all active judges between 1999 and 2004. Similarly, in 2001 and 2002, Premier Oil organised a series of nine human rights workshops in Burma. These were run by specialist human rights lawyers hired by Premier. About 250 participants from the army, police, energy ministry, labour and immigration departments were taught in two-day seminars about human rights issues.

‘Fenceline’ communities

Fenceline communities – those villages and towns immediately adjacent to mines, factories and other facilities – have long been on the corporate agenda. Historically a company might have regarded its fenceline communities as a labour source, and may have provided certain benefits to the town through its programme of philanthropic giving.

This relationship is now much more complicated. To begin with, companies have begun to realise that promoting a positive relationship with the local community can be valuable in terms of physical security – a community that broadly welcomes the presence of your site is less likely to damage it. However, the most significant shift is in what needs to be part of this ‘positive relationship’.

Mining firms in particular report that a ‘positive relationship’ now means providing genuine long-term value to fenceline communities. This means providing, not just unskilled jobs, but skilled openings as well – and the training needed to be able to apply for them and get them too. Further, it means using local suppliers as part of a strategy to build a local economy that is more diversified than just the mine site. In the long-term, it means proactively planning for what will happen when the mine closes: where will employment and wealth-creation opportunities come from when the site shuts?

The result is that many companies are applying considerable effort to understanding and responding to their local communities. Anglo-American has developed its ‘SEAT’ tool (Socio-Economic Assessment Tool) to help its managers understand and respond to the needs and expectations of local communities. Shell has a department specifically tasked with understanding the tensions between their operational sites and local people.

Ethics

How companies behave, how they govern themselves, and transparency over their processes have all become much more significant as requirements of companies.

Corruption

Whatever the rights and wrongs of the initial case itself, the UK Government’s decision to halt the Serious Fraud Office’s investigation into BAe System’s Al Yamamah arms deal with Saudi Arabia was highly illustrative. The circumstances served to illustrate the complexity of the corruption issue, and how damaging to a company’s reputation can be the implication that it is embroiled in unsavoury practices.

Some argued that, in pulling the enquiry, the Blair administration had undermining the international community's campaign against corruption. Others argued that, if BAE had paid bribes, this was justifiable since it safe-guarded British jobs. Others again pointed to the correlation between countries that are corrupt and those where human rights abuses occur.

There is little doubt that in some industries and some countries, corruption has been tolerated: it is seen as something that needs to be dealt with if business is to be done. What is apparent now is that embroilment with corruption both damages a company's reputation and leaves its directors open to legal challenge. The problem, of course, lies in how to identify where in a company's operations corruption may occur and, when identified, how best to tackle it.

EITI

The Extractive Industries Transparency Initiative is an excellent example of an attempt to tackle corruption in business practice. The Initiative was established to demonstrate that payments due to governments under extractive production sharing agreements were made to the country's exchequer, not to individual ministers or officials.

However, the nature of the EITI itself reflects new processes of collaboration in which companies need to engage. The process was initiated by the British and US governments, but those active in it include leading extractive companies, campaign groups, and governments both of home and host countries. The process is run by a Secretariat based in Oslo. As a result, companies are having to work closely with organisations very different from themselves in aims, culture and structure.

Governance

In the UK, a series of reviews in the past two decades have made recommendations that have significantly changed the norms of corporate governance, and the responsibilities of boards of directors. The Combined Code of Corporate Governance establishes a clear set of expectations about how companies ought to run themselves. If they do not comply, they have to explain in their annual report why they do not.

Arguably, corporate governance will be under even greater scrutiny in the next few months in the light of the financial crisis. Arguably, the current problems were precipitated by an entire sector – finance and banking – failing to govern itself responsibly and in a way that contributes to the good of wider society. It is likely that in many jurisdictions tighter regulations will be introduced to ensure that a similar situation cannot arise again.

Raising the bar

It seems unlikely that these issues, and the complexity to which they give rise, are about to disappear. Many of these factors arise from trends of globalisation, and as such are inherent in the decisions companies make to operate in new markets. However, the expectations others have of corporate behaviours are also rising.

In the UK, the Leader of the Opposition, and likely next Prime Minister, David Cameron has said that he wants “the modern Conservative Party to be not just the party of business but of responsible business.” The policy group he established to examine responsible business practice made a number of recommendations about what a future Conservative Government could do “to encourage business to play a central role in securing a better future for British society”.

On the international stage, Professor John Ruggie’s mandate has been extended as UN Secretary-General’s Special Representative on Business and Human Rights. Earlier in 2008 Ruggie had made a number of recommendations as to how companies might be held to account for human rights. His on-going work will test these recommendations.

In the area of corruption, leading economies are under pressure – particularly in light of the BAe Systems altercation – to strengthen their legal strictures against corruption and to ensure that the OECD conventions against corruption are fully reflected in their national laws.

If these issues are not going away, then companies need to learn how best to deal with them, and to manage them effectively.

Challenges

However doing this presents novel challenges to corporate managers and leaders. These social, environmental and ethical conundrums are by definition new to most people and much of the usual machinery of management is ill-suited to deal with them effectively. There are a number of key challenges, which include the following:

- **Lack of clarity**

It is often very difficult to get to the bottom of these issues, or to be certain that all relevant factors have been taken into account. At times, it can be a challenge even to know what the question is, much less to be certain about what the answer might be.

- **Absence of a clear answer**

When taking decisions on, for example technological issues, there is ‘an answer’ to questions that might be posed. In dealing with social, ethical and environmental issues, there is rarely such a clear answer.

- **Taking decisions on incomplete information**

Rarely will it be possible to ensure that all relevant information has been gathered on which to base even very important decisions. Managers are challenged to take decisions on the back of incomplete information.

- **Dealing with strange issues**

As the above indicates, companies are increasingly finding themselves required to deal with issues – human rights, for instance – that in the past would not have been seen as relevant to them. Realising that these issues are now on the corporate agenda, and then getting up to speed on them both represent significant challenges.

- **Dealing with people not like you**

Moreover, managing in this new environment requires an ability to develop relationships with NGOs, campaigners, local communities and many other 'non-traditional' groups. Most corporate managers and leaders are very unused to dealing with people 'not like them'.

- **Misfit with corporate systems and practices.**

Most corporate systems are quite linear, and rely on clarity, a measured process of information gathering and decision-making: things that can be fitted into an Excel spreadsheet. These new issues are not linear, they are complex and inter-locking. They most certainly fit ill in a spreadsheet.

- **The unknown unknowns**

Donald Rumsfeld was right: the things you don't know that you don't know can have a huge impact on your business. However, an NGO campaign can be launched against you; issues may arise in your supply chain: your business plan needs to be able to respond.

Henley's response

A number of business schools are seeking to help their client companies address these issues: Henley is no exception.

Other business schools have established centres dedicated to CR and sustainability. Examples include the International Centre for Corporate Social Responsibility at Nottingham; Ashridge's Centre for Business and Society; and the recently-established Doughty School at Cranfield.

We are exploring a slightly different approach from these and others of our peers

We believe that success in managing these issues lies, not in developing a cadre of CR/ sustainability managers, but in developing mainstream management professionals and leaders capable with dealing with complexity and handling societal, ethical and environmental issues as part of their day-to-day business practices.

Specialist input will always be needed, and organisations will need to retain experts in those aspects of the CR and sustainability agenda relevant to them. However, it will not be these specialist that solve these issues, or manage the impacts that they have on the organisation. That will be done by the line managers who already run the business. CR and sustainability in the supply chain needs to be managed by procurement professionals; the issues that arise from plant operations will be managed by the managers of those sites; and the issues that arise from doing business in new markets will be addressed by the leaders of those operations.

Henley is therefore exploring how it might build on its existing expertise in leadership development and behaviour change to help develop managers and leaders capable of dealing with complexity, and with environmental, societal and ethical issues. Potential interventions may include:

- **Leading a Sustainable Organisation**

A tailored programme focussed on the industry- or functional-specific issues of the CR/ sustainability agenda

- **Integration into the Advanced Management Programme**

Ensuring that sustainability/ CR issues are incorporated into the structure and content of the AMP

- **Coaching**

On-going support to managers and leaders in their work context

- **Immersion training**

Allowing participants to ‘walk a mile in someone else’s shoes’

- **Communities of practice**

A gradually-expanding community of practitioners who can share their experiences and learn from each other.

- **Conferences/ seminars**

Regular events to showcase best-practice, new thinking and provide access to leading specialists.

- **Research**

Examining in detail specific aspects and issues of the agenda, and how leading companies are managing them.

We are currently undertaking a process of research and consultation to refine our thinking and to define a more specific range of interventions. Accordingly, we would very much welcome any comments or observations that people might have, to:

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Peter Davis



Peter Davis is a specialist with more than 15 years experience in the fields of corporate responsibility (CR), political and societal risk and business ethics. He advises a wide range of companies as varied as Shell, BSkyB and Diageo. Recent projects include working with Anglo-American on development of their long-term sustainable development strategy; integrating ethical, environmental and social issues into the procurement system of British Land; developing an ethical procurement policy for Northrop Grumman; and coaching Lafarge's subsidiaries in Nigeria on business ethics.

Peter is Political Editor of Ethical Corporation, and writes widely on the social and political issues underlying the corporate responsibility agenda. Recent articles can be found in the politics section of www.ethicalcorp.com.

He is also co-director of the *Ethical Corporation* Institute, which provides researched-backed recommendations to companies on how to adapt to their changing role in society. His ECI paper *Companies in Post-Conflict Reconstruction: Learning from the Wider Agenda* was published in February 2008.

As well as working on understanding the issues, Peter works with company boards and managers to help them to respond to the new challenges posed by CR. He is currently training the senior staff of a large American corporation to respond to the ethical challenges posed by their new business activities in China.

For the past 2 years, Peter has chaired the Working Group on Responsible Business for the UK Conservative Party. He wrote the Group's mid-term report, published in January 2007. The final report, *A Light but Effective Touch* was launched by Peter, Leader of the Opposition, David Cameron and leading shadow cabinet members in March 2008. He is now working with former CEO of Asda, Archie Norman to carry forward the Working Group's recommendations.

From 1994 to 1997 Peter was Operations Director of the Prince of Wales Business Leaders Forum, and established the organisation's operations in Russia, southern Africa, China and Vietnam.

Previously, he worked for NATO developing good demographic practice in the countries of the former Warsaw Pact.

He was educated at the University of Oxford and is currently completing a PhD examining the role of corporations in post-conflict environments at London University. He is a Fellow of the Royal Society of Arts and of the Royal Geographical Society.

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