MAKING THE BUSINESS CASE FOR SUSTAINABLE DEVELOPMENT

Introduction
A member of the Charles River Printing Board of Directors, Harriett Watson, has become increasingly concerned with the sustainable development activity in the company. Even though Charles River Printing is not publicly traded, board members still have a fiduciary responsibility to see that the company is working in the best interests of its shareholders (i.e., the owners, the employee-owners and others who have invested in the company). She asked a legal expert to talk to the Board of Directors about a term called “corporate governance.” The company’s attorney thought this was a good idea, so Nancy Smith placed the legal expert on the agenda for the next Board meeting.

At the board meeting, the legal expert said that the term, corporate governance, is used to refer to a broad range of rules, regulations, policies and practices that boards of directors use to manage their responsibility to investors and other stakeholders. It is a two-edged sword! On one side there is legal action for not protecting the shareholder’s investment; but, on the other side, there is the threat of the loss of shareholder confidence. A good governance infrastructure should provide higher returns for the shareholder and reinforce the reputation of the company as a sustainable enterprise.

There has been a lot of concern about governance these days. The issues of concern are diverse and include topics such as board diversity, independence, compensation, and accountability, as well as a broad range of corporate responsibility issues such as employment practices, environmental issues and community involvement. Shareholders and the public have renewed their focus on board accountability and increased dialogue about whether voluntary standards are adequate to see that the board addresses these concerns. There has been a call for stronger regulatory solutions. Stakeholders want the board to be pro-active rather than reactive.

The fundamental concerns of corporate governance include:

- ensuring that conditions apply whereby a firm's directors and managers act in the interests of the firm and of its shareholders and even of its workers
- ensuring the means exist to hold managers accountable to investors and employees for the use of assets

Corporate governance specifies the relationships between, and the distribution of rights and responsibilities among, the main groups of participants:
The individuals within the above groups transact with the firm for their own individual purposes, so as the entire group can achieve more mutual benefit than any individual can alone. For instance, directors, workers and management receive salaries, benefits and reputation; whilst shareholders receive capital return. Customers receive goods and services; and suppliers receive compensation for their goods or services. In return, these individuals provide the time, labor, expertise, capital, goods, services, consent, etc required for the organisation to pursue its purpose.

Corporate governance includes:

- the national/regional laws governing the formation of corporate bodies
- the bylaws established by the corporate body itself
- the organisational structure of the corporate body

Corporate governance aims to:

- align the actions of the individual parts of an organization toward aggregate mutual benefit
- provide the means by which each individual part of the organisation can trust that the other parts each make their contribution to the mutual benefit of the organisation and that none gain unfairly at the expense of others
- provide a means by which information can quickly flow between the various stakeholders to ensure that the changing nature of both the stakeholder needs and desires and the environment in which the organisation operates get effectively factored into decision processes.

**Hearing from the Legal Expert**

The expert starts: Historically, many public companies limited their shareholder communications to an annual report, press releases delivered with quarterly financial statements and a scripted presentation at the annual meeting. Shareholders would rarely contact the company to ask questions about corporate performance or new developments. These limited communication programs were sufficient for most companies, which were either controlled or heavily influenced by a significant shareholder or effectively controlled by management where no dominant shareholder existed. Shareholders who became unhappy with corporate performance could simply sell their shares in the market (if publicly traded) or back to the company if private. Many boards of directors
contributed limited real value to companies, providing little more than formal approval for management decisions.

During the 1980's, investors began contributing significant investment dollars to mutual funds and pension funds. These institutional investors became very large, frequently acquiring significant ownership positions in major public companies. In many cases, it became impossible for these investors to sell shares of underperforming companies, either because their substantial holdings could not be liquidated without causing a steep drop in stock price or because of a lack of substitute investment choices for fund managers seeking to track a defined stock index, geographical region or industry group. Institutional investors seeking to improve stock prices of what they identified as underperforming companies began to assert their powers as major shareholders more aggressively. Companies that are not publicly traded are often part of the supply chain of those companies that are traded. Pressure can be exerted on the supply chain to help the customer meet its obligations with its investors.

Fund managers began to demand more timely and more detailed corporate information. Many companies responded by arranging meetings between major shareholders and senior management. Others developed a practice of holding press conferences by conference call to tens (or even hundreds) of analysts and investors in response to corporate developments. The amount and timeliness of corporate disclosure provided to the marketplace -- "information liquidity" -- increased significantly, and large shareholders with the resources to monitor the information flow became more powerful. Institutional investors began to target specific underperforming companies for change and, frequently through the responsive efforts of more active independent directors, achieved significant changes.

Today, investor relations is a high priority for public companies. It is now common to see a steady stream of press releases keeping shareholders up-to-date on business developments. Analysts are in regular contact with company management to stay current on their reports to investors. Stock exchanges now require listed companies to provide comprehensive disclosure of all director relationships and corporate governance practices. The shift in power can be seen in the policy statements now issued by major institutional shareholders (and their representatives) setting out the types of corporate behavior they are prepared to support. Directors are being held increasingly accountable for corporate failures and those who do not take their positions seriously act at their peril.

The trend is clear: as information liquidity increases, shareholders become more powerful and companies are forced to respond. The entire supply chain is often brought into action.

Governments are increasingly getting into the act. First there was the passage of the Sarbanes-Oxley legislation in the United States. The European Union and other governments are getting into the business of watching publicly traded companies in the wake of a large number of financial scandals. It is the way that the environment used to
be. Many new regulations need to be tracked and systems within the company must be changed to adapt to these many new requirements.

All of this activity is making it harder for members of the Board of Directors to get “errors and omission” insurance. People have begun to sue directors with a sharply increased frequency whenever something goes wrong with the financial position of the company. Directors need to be astute to all changes that are occurring and question the management about its decisions that affect the financial position of the company.

**Good governance has 8 major characteristics.** It is participatory, consensus oriented, accountable, transparent, responsive, effective and efficient, equitable and inclusive and follows the rule of law. It assures that corruption is minimized, the views of minorities are taken into account and that the voices of the most vulnerable in society are heard in decision-making. It is also responsive to the present and future needs of society.

**Participation**

Participation by both men and women is a key cornerstone of good governance. Participation could be either direct or through legitimate intermediate institutions or representatives. It is important to point out that representative democracy does not necessarily mean that the concerns of the most vulnerable in society would be taken into consideration in decision making. Participation needs to be informed and organized. This means freedom of association and expression on the one hand and an organized civil society on the other hand.

**Rule of law**

Good governance requires fair legal frameworks that are enforced impartially. It also requires full protection of human rights, particularly those of minorities. Impartial enforcement of laws requires an independent judiciary and an impartial and incorruptible police force.

**Transparency**

Transparency means that decisions taken and their enforcement are done in a manner that follows rules and regulations. It also means that information is freely available and directly accessible to those who will be affected by such decisions and their enforcement. It also means that enough information is provided and that it is provided in easily understandable forms and media.

**Responsiveness**

Good governance requires that institutions and processes try to serve all stakeholders within a reasonable timeframe.
Characteristics of good governance

Consensus oriented

There are several actors and as many viewpoints in a given society. Good governance requires mediation of the different interests in society to reach a broad consensus in society on what is in the best interest of the whole community and how this can be achieved. It also requires a broad and long-term perspective on what is needed for sustainable human development and how to achieve the goals of such development. This can only result from an understanding of the historical, cultural and social contexts of a given society or community.

Equity and inclusiveness

A society’s well being depends on ensuring that all its members feel that they have a stake in it and do not feel excluded from the mainstream of society. This requires all groups, but particularly the most vulnerable, have opportunities to improve or maintain their well being.

Effectiveness and efficiency

Good governance means that processes and institutions produce results that meet the needs of society while making the best use of resources at their disposal. The concept of efficiency in the context of good governance also covers the sustainable use of natural resources and the protection of the environment.

Accountability

Accountability is a key requirement of good governance. Not only governmental institutions but also the private sector and civil society organizations must be accountable to the public and to their institutional stakeholders. Who is accountable to whom varies depending on whether decisions or actions taken are internal or external to an organization or institution. In general an organization or an institution is accountable to
those who will be affected by its decisions or actions. Accountability cannot be enforced without transparency and the rule of law.

“It is my recommendation that the Board of Directors form a committee to address social responsibility and to hold the management of the firm accountable for upholding the fiscal position of the company whenever seeking to address this issue.”

Ms. Watson thanked the expert for coming and sharing an opinion on what the Board should do with the drive to institute a sustainable development program and the risk that it might bring to the organization.

Charlie Smith thanked Ms. Watson for inviting the expert and for sharing her opinion with the Board of Directors. Then he recognized another board member to speak, his wife.

**Hearing from the Largest Investor**

Nancy Smith thanked the legal expert and board member Harriett Watson for the excellent briefing. She then provided a briefing to the board on some of the issues associated with the developing sustainable development program

1. By following the Systems Approach to process improvement, all of the projects that will be included in the sustainable development program will be approved by the management oversight team based on the following factors:
   a. Demonstrated ability to have a positive effect on the bottom line as demonstrated by a cost/benefit determination that is built into the employee-prepared action plan
   b. Giving the employee owners a sense of how their actions affect the bottom line of the organization
   c. Ability of the projects to address the **interests** raised by the company’s key stakeholders and a plan to close the look with those stakeholders as the project begins to satisfy those interests
   d. The level of personal commitment shown by the employees on the team and how they will use their energies to improve the productivity factor at Charles River Printing both by their contributions to the project and by providing an example for other employees to follow
   e. Through the lessons learned on the project, the employees are challenged to demonstrate how the company can leverage their top line (revenues and brand) by staying ahead of the competition and winning the business of new customers.

2. The Bank of America is a key stakeholder for Charles River Printing as they have provided a line of credit that helps us expand our business. The bank has a firm commitment to the environment. They require all of the bank associates to support their environmental goals. Lately they have embarked on a program to

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1 Bank of America Commitment to the Environment; [http://www.bankofamerica.com/environment/index.cfm](http://www.bankofamerica.com/environment/index.cfm)
encourage sustainable development by integrating their social programs with the environmental programs. As a result of a referral made by their local loan officer, Charles River Printing has been in contact with the corporate people in Charlotte, North Carolina, as a possible benchmark candidate. The corporate office is currently negotiating a printing contract with Charles River Printing because they want to encourage sustainable businesses.

3. The project to use less flammable solvent has been shown to their insurance carrier, The Hartford. Although The Hartford has an exemplary community service program, its re-insurer, Swiss Re, has requested that they develop some kind of sustainable development program. Swiss Re² has become quite active in promoting the lowering of greenhouse gas emissions both in their own operations and in the operations of all of the insurance companies that they provide re-insurance support. The Hartford has provided a reduction in the amount of premium it collects on our insurance policy and has asked for regular briefings on the status of our program. We are talking to them about a printing contract.

4. Charles River Printing has just been nominated for a recognition program in the City of Cambridge called the “Go Green Award³.” There is a new energy category. The announcement of the awards will be made in May. The City has awarded Charles River Printing a contract to prepare the brochures for the Go Green Month⁴ promotion. Charles River Printing will hold some tours and open house events to feature how it has reduced the amount of energy by eliminating the need for air pollution control equipment when it reduced the amount of solvents used in their inks and for cleaning the presses. The City of Cambridge is a key stakeholder. Our expansion plans require a number of permits and approvals from the City. We hope that our reputation as a key player in some of the proactive programs sponsored by the city will help expedite these approvals. Recognition from the City is also good for our business and will be used by our marketing people to promote our business with a citizenry that is very accepting of sustainable development and what it means at the local level.

5. All the employee projects in the sustainable development program are carefully selected and formulated to save more money that they cost. Employees will have to charge all time and materials to their projects and will only be able to claim benefits against these costs that have been pre-approved by the accountant and the management oversight committee. This is not a “feel good” effort. We are doing it because it will make us stronger financially.

6. The management oversight welcomes the active involvement of the Board of Directors. I would like to show you a figure that describes how the Board and senior management help bound the whole system. We see the sustainable development program as part of our set of internal controls where they address the

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² Swiss Re Climate Protection Program; [http://www.swissre.com/](http://www.swissre.com/)
interests of our key stakeholders, including the members of the Board of Directors. It is also the best form of risk management because it is focused on preventive action, not reactive actions.

Nancy Smith then made a motion to have the Board of Directors establish a Board Committee to provide oversight of the Charles River Printing sustainable development program. She suggested that Ms. Harriett Watson serve on that committee and act as its chair. As a point of discussion, Charlie Smith asked Ms. Watson if she would serve the Board in this way. She assented. The motion was seconded and passed by a unanimous consent. Ms. Watson was asked to suggest two members to serve with her and report on this at the next meeting. Nancy Smith was asked to represent the management oversight committee of the sustainable development team and provide a full accounting of the project and the results obtained to date so that it can be reviewed at the next meeting.

The meeting was adjourned.

**Questions to Address**  
The weekly discussion should focus on the following questions:

How should projects use the “tactics” presented in the past two weeks to demonstrate their financial independence and contribution to both the bottom line and the top line (revenue/brand) of the company? How should this information be presented to this new
Board committee that will be providing the ultimate oversight of the sustainable development program?

How does the sustainable development program meet the eight major characteristics of good governance?

Each of the three responsibilities had management systems that would help to structure the programs and are auditable and certifiable by independent third parties. Would it make any sense for the company to institute and integrate these management systems and have them independently audited so the results could be reported to this new Board committee? Or could the results of the project efforts be sufficient to have the Board committee feeling comfortable that they are meeting their fiduciary responsibilities? What would be a major risk that the sustainable development program could pose to the board?