Confederation of Indian Industry

CII-ITC Centre of Excellence
for Sustainable Development

THE NEXT IN CORPORATE GOVERNANCE:

SUSTAINABILITY EMBEDDED

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The Next in Corporate Governance: Sustainability Embedded

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Preface

This report is a call-to-action. It was ideated in the backdrop of widespread call for a retake at capitalism and particularly business conduct post-Lehman Brothers and post-Satyam. So strong has been its impact, that despite the soaring economies in Asia and parts of Europe in 2010, business leaders continue to call for business responsibility to global challenges and accountability to stakeholders. According to CEO of Nestle SA, "This was not a financial crisis, but a value crisis, where greed replaced ambition and confidence became arrogance." He was one of the many at WEF 2011 at Davos, signalling a shift from share value to shared value.

This report was being finalised while CEOs and thinkers were echoing similar views. It strengthened our belief that such shift could happen only if sustainability was embedded in corporate governance. It is not sufficient to embed sustainability in operations, but needs to be reflected in how an enterprise was governed.

That sounds logical and reasonable. That was the starting point for the interface framework presented in this report.

This report begins with the business case for sustainability quickly followed by the board case. It then provides a review of corporate governance and its mishaps both in developed countries as well as India. The report then presents the framework.

The framework has three key elements: board diversity, policy frameworks, and performance evaluation. It embeds sustainability to what boards already do as against adding sustainability as a new dimension.

We hope this report will induce discussion on the subject. There will be no single view and there will be disagreements. We welcome debate on the subject and particularly the framework as an indication that there is a realisation that Board functions need to embed sustainability beyond lip-service. We acknowledge that resistance to change is only fair. But change-makers are our encouragement and we will continue to work with them to see this interface happen in the real world.

Seema Arora
Executive Director
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[1] Damodaran.H., 2011. From share value to shared value [Online] (Updated 29 January 2011) Available at: http://www.thehindubusinessline.in/2011/01/30/stories/2011013050880700.htm [Accessed 30 January 2011]

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1

Developing Case to Embed Sustainability

It does make business sense to embed sustainability into corporate governance

The primary purpose of companies is to maximize shareholders wealth and supply goods and services to the customer. While bearing this purpose of its existence it has to execute many functions. These include delivery of products and services as per customer's needs. For this it has to tap existing and new markets with the help of sales and marketing functions in a manner that enhances brand equity and reputation. They employ adept manpower, train and skill them for a suitable jobs, build infrastructure and deploy technology, design and implement competitive strategy, counter risks to avoid major losses and foresee overall functioning according to set rules and regulations.

This is the way business is done and it involves a web of departments, human resources, technology, and infrastructure. Risk management is an essential ingredient towards reaching this desired purpose. It comes in many forms: natural calamity like floods, cyclones, air pollution, disasters due to climate change, company specific risks like labour unrest, corporate fraud, money laundering and many more. Company's success rests on how it mitigates these risks and avoids any pitfalls that threaten its value and equity.

It is the responsibility of boards along with CEO and chairman to direct the company to move in a particular direction. Thus their function within the company is of utmost importance. They govern the company by establishing broad policies and objectives, ensure the availability of adequate financial resources, approve budgets, and account to stakeholders for organizations performance. This function is very well termed as "Corporate Governance".

Within the framework of corporate governance boards look at various issues affecting the company, its policies and objectives. It is also the backbone of any company which is a visage for any crisis and risk to knock on. It is important that the framework of sustainable business and corporate governance takes into account such risks within its functioning and mitigate their affect. Risks do not only affect companies but in varied forms affect society, economy and environment.

To manage such risks, continue to grow and remain relevant to changing markets, companies have to reinvent and reorganise themselves. According to an analysis conducted by the CII-ITC Centre of Excellence for Sustainable Development, over the period of four decades (from 1970 to 2010) 407 new companies have been added to the list of Fortune 500 companies. This means that around 407 companies of 1970 have lost it to Fortune 500 list in 2010. One reason can be increased competition from new companies or existing companies with better and enhanced working style; others can be mergers, acquisition, bankruptcy, etc.

Companies should reinvent in a manner that defines or responds to evolving sustainability trends and indicators. Sustainability is increasingly becoming the norm of economic growth and consumer lifestyles. It is not just about becoming green. Sustainability goes beyond climate change and greener planet to include socio-economic wellbeing of all people. Companies need completely different work-styles and business models that embrace economic, social and environmental issues and indicators in business strategies.

These new formats of business require sustainability to be embedded into corporate governance. Unless that happens, reinvention and reorganisation of companies is unlikely to take place successfully.

This report provides a framework to embed sustainability into corporate governance. The framework details various elements of sustainability and corporate governance.

Framework for integration of corporate governance and sustainability not only focuses on the functioning of boards but also on the functioning of senior management. The management of the company ensures that the objectives of the company are met. Strategies are developed by senior management, their implementation is monitored by boards, and result sensed by stakeholders. These three parties are integral to corporate governance.

Evolution of Corporate Governance Reforms

Legend	Indian Reforms	International Reforms	Scandals

1990	Polly Peck			
1991				
1992	Cadbury committee	Stock Market Scam - India		
1993				
1994				
1995	Greenbury committee			
1996	CalPERS			
1997	Asian Financial Crises			
1998	CII Code			
1999	OECD Principles			
2000	Birla committee, Clause 49			
2001				
2002	Narayan Murthy committee	Naresh Chandra committee	Sarbanes-Oxley act	Enron, AOL, Adelphia, Tyco, WorldCom
2003	Higgs Report	Parmalat		
2004	AIG			
2005				
2006				
2007				
2008				
2009	Corporate Governance Voluntary code guidelines	Satyam Computer Services		
2010	Lehman Brothers			

CESD Analysis

History of Reform Process

The Indian economy and financial markets underwent radical reforms in the early 1990s, largely in response to the country's economic crisis in the late 1980s. The reforms caused extensive change to the Indian capital market and its corporate governance landscape. In 1992 the Securities and Exchange Board of India (SEBI) was established with a mandate to protect investors and improve transparency in the securities market, and led to securities regulation by this autonomous body. In India the initial impetus for corporate governance reform was driven by the private sector, which was keen to make Indian business more competitive and respected in global markets. The Confederation of Indian Industries (CII) published a voluntary Code of Corporate Governance in 1998. The SEBI followed by setting up the Birla Committee on Corporate Governance, and its December 1999 recommendations formed the basis for Clause 49 of the SEBI Listing Agreement. The Birla committee recommendations sought guidance from the 1992 Cadbury report in the UK and, as a consequence, India adopted key planks of an 'international best practice' code. SEBI revised Clause 49 introduced in late 2004, with the revisions to the independence of the chair and proportion of independent directors coming into effect on 1 January 2006. Since 2006, listed companies are required to submit quarterly compliance reports to the SEBI, similar to those required in the US by Sarbanes-Oxley

Source: *Lange, H. & Sahu, C.,2008. Board Structure and Size: The Impact of Changes to Clause 49 in India. August 2008, Singapore*

2

Learning from Fault lines in Corporate Governance

As a result of this economic reform and development process over the past 20 years India produced many highly regarded companies in sectors such as information technology, banking, automobile, steel and textile,. The idea was to respond suitably to the developments taking place world over. These companies are now making their presence felt outside through global mergers and acquisitions. They are also competing with MNCs of developed countries in terms of quality and cost.

The reform process in corporate sector had many causes. One, the global cases on corporate fraud and financial meltdowns led the corporations worldwide, including India to take a deeper look at the existing framework of corporate governance. Two, the 1992 stock market scam was an eye-opener towards bringing the issue of corporate governance to the centre-stage, to protect the interests of shareholders and to build confidence of foreign financial institutions in the Indian capital market.

The world has witnessed corporate scandals in many forms; Enron, Tyco, Worldcom, Parmalat, Lehman Brothers to name a few. Taking a glimpse at the international corporate failures, Enron is an excellent example where those at the top allowed culture to flourish in which secrecy, rule-breaking and fraudulent behaviour were acceptable. Enron had all the structures and mechanisms for good corporate governance. In addition, it had a corporate social responsibility task force and a code of conduct on security, human rights, social investment and public engagement. Yet no one followed the code[2]. The Board of directors allowed the management openly to violate the code. Enron collapse erased billions of dollars of market value, wiping out huge savings and taking away thousands of jobs.

In 2004 Italy's eighth-largest company, Parmalat went dizzy on account of false transactions. The illegal acts were carried out worldwide and they affected not only the company and its people but international financial institutions as well[3].

In case of Tyco International the company's funds were misused by the CEO and CFO of the company. They even tried improper accounting practices to cover up the misuse of funds. AIG, one of the foremost insurance companies in the US inflated the company's net worth by $2.7 billion[4]. These international corporate disasters have regularly questioned Board and senior management in terms of their role while the company was involved in the unlawful acts. This has also led governments and committees world over to take up a stricter view of corporate governance.

India too is a witness of corporate frauds, recent one being Satyam crises in 2009. In this case, Ramalinga Raju of Satyam was inflating the books for revenue and profit shortfall. Later, when he was charged with conspiracy, cheating and forgery it had a crippling impact on the company and on its stakeholders. The betrayal of trust impacted not only the employees but the entire Indian tech services industry. Disaster like this impacts the credibility in the overseas market which Indian tech services industry has built over 20 years. Another major impact was on Byraju Foundation, a non-profit organization of Satyam, aimed at bringing economic development to farm communities in the state of Andhra Pradesh. After the collapse around 350 employees of Byraju left the company.

After the fiasco the Board was questioned and it turned out that they had no clue of what was happening at the management level. The lesson learnt is tighter role of Board in corporations. The question here is even if we improvise the role of the Board from strong to stronger, are we giving them enough weapons to counter the challenges they face.

The affect of such jolts is felt on the overall economy of the country; sometimes it has worldwide repercussions, like the one faced worldwide due to Lehman Brothers debacle. The ill-affects are also faced by the society, with betrayal of trust for corporate, loss of finances, etc. However restricting ourselves to corporate failures due to financial fraud will not be fair to the whole concept of corporate governance. The crisis creeps through every door. It can be a corporate fraud, scams, factory blast, oil spill, toxic sludge spill, environment disasters, etc. This indicates that any major move by a corporate has both negative and positive affect not only on the company but also on the economy, society, and environment of a country.

Crises happening at international level also provide an example which can be repeated anywhere, even in India. The British Petroleum oil spill not just distressed the company in terms of human lives lost and financial loss from investor's sentiments and infrastructure. The spill also caused extensive damage to marine and wildlife including several birds, sea turtles, fish, and mammals. The company incurred huge expenditure as a result of cost of the spill response, containment, relief well drilling, grants to Gulf States, claims paid, and federal costs. Later when the investigations were done some astonishing facts came to limelight with British Petroleum taking the onus of the spill, along with Transocean, who owned the oil rig. The facts included negligent behaviour, ignored warnings, and misinterpretation of data. These reasons could have been well avoided with a proactive approach by the company, thus avoiding major disaster and saving the lives, environment, and economy.

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[2] Mehta, S. & Srivastavaare, R., 2009. Reasons for Corporate Governance Failure [Online] (Updated 18 March, 2009) Available at: http://www.indianmba.com/Faculty_Column/FC974/fc974.html [Accessed 20 November, 2010]

[3] Emi. 10 Scandals that Rocked the Accounting World [Online] Available at: http://hubpages.com/hub/10-Scandals-That-Rocked-the-Accounting-World [Accessed 20 November 2010]

[4] Ibid

Had these companies been a bit more sensitive about the consequences such disasters have, their leadership group level including the Board and senior management would have integrated sustainability with the overall corporate governance. These examples clearly indicate two things. First, opportunities for companies to audit their current operating framework and look for any loopholes which can lead to disaster affecting the human and ecosystem. Second, development of framework integrating triple-bottom-line with corporate governance

The fast paced corporate world has seen many such chapters unfolding. It is important to gain lessons from such examples and move forward with a new approach to success. The new approach requires integration of economic, social and environment issues within corporate governance.

Effective corporate governance requires a proactive, focused state of mind on the part of directors, the CEO and senior management, who all must be committed to business success through maintenance of the highest standards of responsibility and ethics. Even the most thoughtful and well-drafted policies and procedures are destined to fail if directors and management are not committed to enforcing them in practice.

The framework for corporate governance is not only an important component affecting the long-term prosperity of companies; it is also a leading species of large genus namely, National Governance, Human Governance, Societal Governance, Economic Governance and Political Governance[5]. All of this is also a part of sustainability. Sustainability encompasses various issues including, environment, health, safety, corporate social responsibility, philanthropy, community, etc. A sustainable corporation is the one that protects the environment and improve the lives of those with whom it interacts, while creating profits for its shareholders. This definition of sustainable corporation is achievable when the triple-bottom-line (economic, social, environment) is well integrated into the framework of corporate governance.

[5] Verma, S.k., Gupta, S., 2004. Corporate Governance and Corporate Law Reform in India, IDE Asian Law Series No. 25, Institute of Developing Economies.

3

Sustainability in Practice – Indian Examples

It is time to take a fresh perspective on the status of sustainability in corporate India. Sustainability has many aspects. It should be seen in tandem with different business functions. A marketing director looks at sustainability from a different perspective than a financial director. With this thought sustainability cannot be limited to just a few individuals within an organization, where they look at this subject as only community development or philanthropy. In the previous section few examples gave a clear picture of how companies failed due to negligent behaviour towards governance. However there are companies which have learnt the lessons and are moving forward leaving behind a trail for those who want to be followers and for those who want to take bits from this success and build there own success trail with innovation and leadership.

Fostering this path is Infosys. Founded by N.R.Narayana Murthy in the year 1981, the company within its 30 years of operations has achieved a status of excellence not only in terms of its business operations but also as an excellent corporate citizen. Till the year 2009 the company was operating on the principle of Predictable, Sustainable, Profitable and De-risked (PSPD) model. A successful and smooth sailing through this model further pushed the company to have consolidated sustainability strategy model in the year 2010. This well-defined sustainability policy complements other policies in the organisation. The objective of the policy is to become a responsible, leading global organization working towards the greater common good by setting global benchmarks for a sustainable tomorrow.

The sustainability policy works in concert with various other policies which exists within Infosys. It follows the philosophy of maximizing value to company's stakeholders; clients, employees, investors, vendor partners and the society, while adhering to company's values. The sustainability agenda of the company is in three areas: social contract – working towards equitable society, ensuring resource efficiency – by being responsible consumer of energy and natural resources and green innovation – by developing sustainable solutions to reduce carbon footprint of their customers[6].

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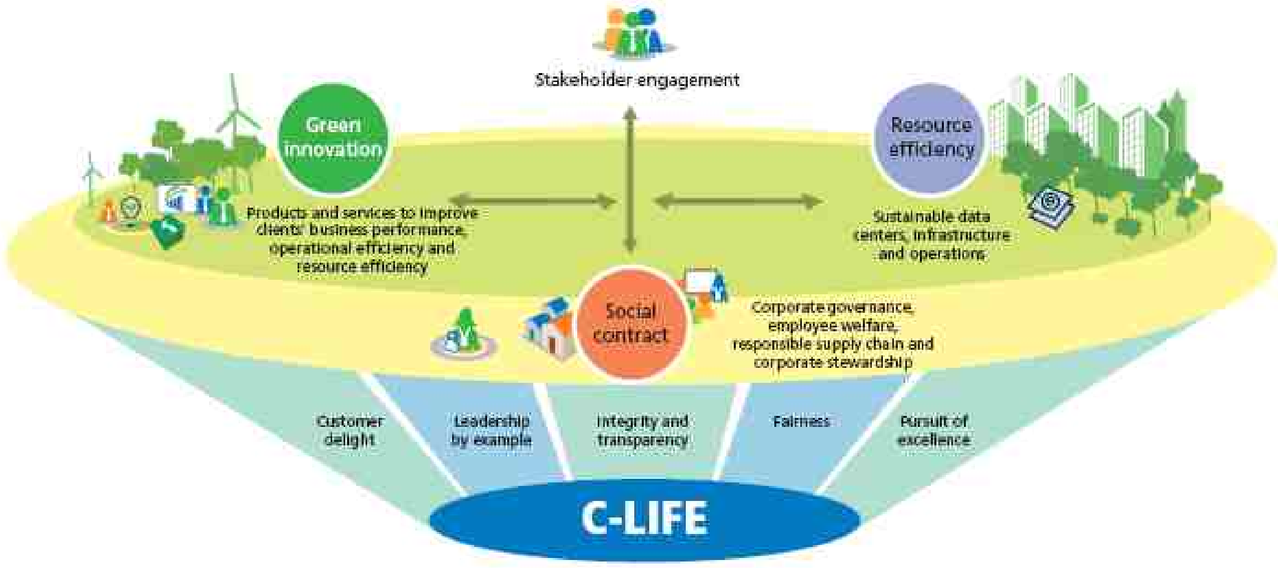
[5] Infosys. (2010). Sustainable Tomorrow, Sustainability Report 2009-10



The company also has Sustainability Executive Council (ISEC) which looks at the strategic implementation of business, environmental and social goals and code of ethics. The members of the council are drawn from branding, business, diversity, environment, finance, human resources, infrastructure, training and quality.

Wipro is another example which has taken sustainability seriously. Wipro says "Sustainability is not just about protecting our natural environment; it also involves creating a better community, promoting a vibrant social network and reviving economic growth. Wipro's sustainability initiatives are based on the belief that businesses today have a clear responsibility to contribute to the creation of a just, equitable and humane society[7]."

At Wipro sustainability is not a separate function with limited definition rather it's a part and parcel of each and every process within the organization, involving all the stakeholders concerned. The firm believes that the building blocks of sustainability includes the government, civil society, customer and suppliers other that the company itself. The sustainability dimensions which the company considers and works around include energy and GHG intensity, water efficiency, waste recycling and pollution mitigation, employee health and safety, diversity, people development, IT for green, education and community initiative[8].

With such dimensions the responsibility for sustainability spread across all levels within the organization – from Board of Directors to voluntary employee chapters. The role of each of the organizational entity is explained in the corresponding table.

[7] Wipro (2009). Sustainability Report, 2008-09
[8] Ibid

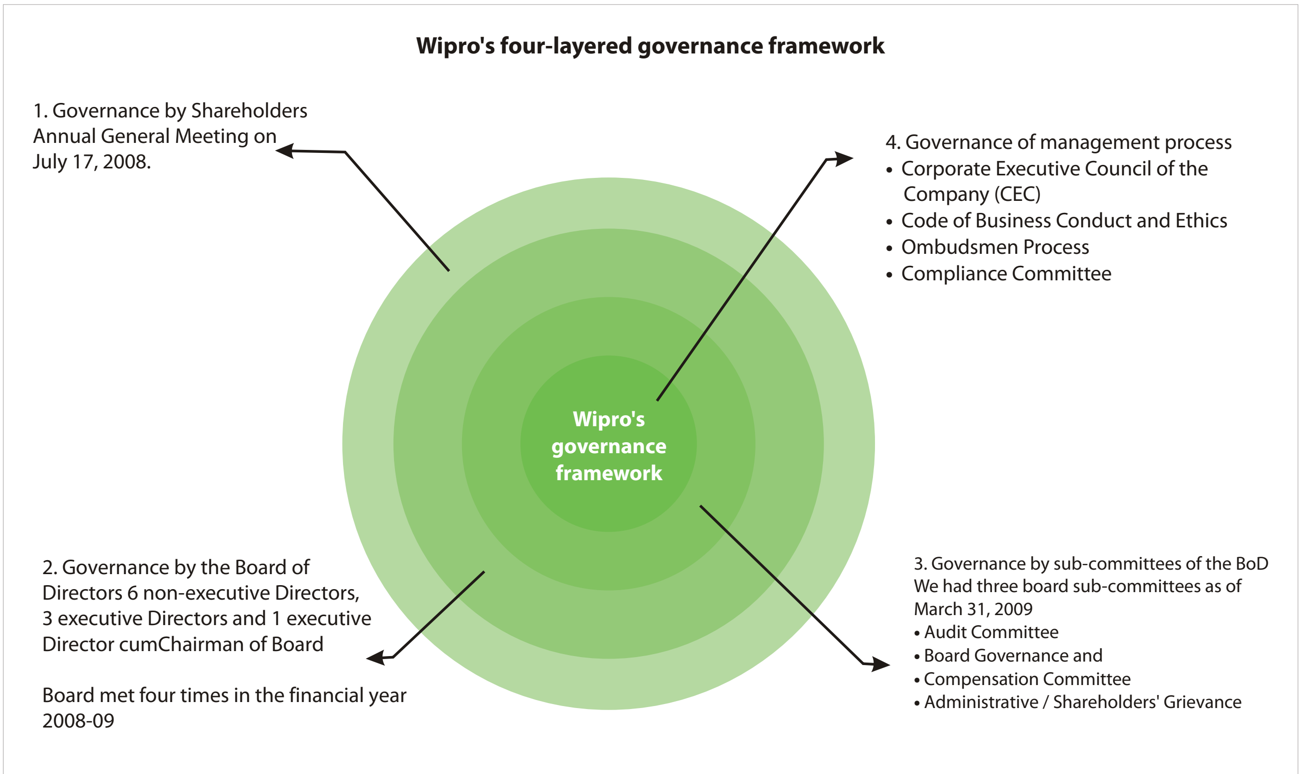
Organizational entity	Principal role and function
The Chairman and the Board of Directors (BoD)	The Board of Directors (BoD) is the senior-most governance body that reviews the progress of the overall Sustainability program once a quarter as part of the review cycle of the company's quarterly performance.
Corporate Executive Council (CEC)	The Corporate Executive Council (CEC) is the top executive governance body of Wipro comprising the Chairman, the two joint CEOs of the IT business, the CFO, the Executive Vice President (HR), the Chief Delivery Officer, the global head of consulting and the CEOs of Wipro Infrastructure Engineering and Wipro Consumer Care and Lighting (WCCLG). The CEC takes part in the goal setting as the final approver of the organizational goals on Sustainability. The CEC also reviews the progress of the Sustainability program once a quarter. One of the CEC members, Mr Anurag Behar holds overall responsibility for Wipro's Sustainability charter, social and community programs.
eco-eye Sustainability program office	eco-eye is the corporate Sustainability program that orchestrates the corporation's Sustainability program from planning to evangelizing, execution and review.
Facilities Management Group (FMG)	FMG is the custodian responsible for all Wipro facilities. The execution of most of Wipro's green initiatives in energy efficiency and renewable energy is FMG's responsibility.
Infrastructure Creation Group (ICG)	ICG is responsible for the design and construction of new facilities; they are thus responsible for incorporating the design principles of green buildings (LEED and similar standards) into all new campuses.
Human Resources (HR)	The HR group has a direct role to play in the Sustainability initiatives in diversity, health and safety, employee development etc. In addition, the HR group plays an important role in employee evangelization and in the design and articulation of the Sustainability report.
Finance	Finance carries the responsibility of laying down guidelines for the evaluation of all green investments. They thus carry oversight of the progress towards Wipro's goals in GHG reductions where significant investment is called for. As the custodian of investor relations, our economic performance and the enterprise risk management office, finance is a crucial stakeholder in the Sustainability reporting process.
Business Leadership	The divisional business leaders at the senior most levels play the role of positioning Wipro's green products and services with our customers. They are directly responsible for the success of our customer engagement on our Sustainability portfolio. In addition, they are responsible for advocacy in public networks and forums and for evangelizing the Sustainability message inside Wipro.
Social and Community Programs	Wipro Applying Thought in Schools (WATIS) which works with partners on systemic reform in the Indian school education system has recently started focusing on how to make ecology axiomatic to children's education. Wipro Cares works with communities that are proximate to our operational centers in the areas of ecology, education and health that affect the marginalized groups e.g. reduced access to drinking water because of mushrooming urbanization.
Employee Chapters	The employee chapters are voluntary forums of employees who are passionate about ecological Sustainability. The primary role of the chapters is to evangelize and spread awareness among employees and to participate in multiple activities within the organizational context and with external communities.
Corporate Brand, Communication and Corporate Affairs	The corporate brand, communication and corporate affair groups are three distinct groups. The first two are responsible for enhancing the equity of the Wipro corporate brand and play a crucial role in emphasizing on Sustainability as an integral part of the company's identity and brand. The corporate affairs group works with governments at the central and state levels as well as with policy organizations in influencing policies that serve the green cause effectively.

The corporate governance model of Wipro at the Board of Directors level follows the four-layer framework. This include; Governance by shareholders at the outermost layer, governance by the Board of Directors forms the second layer, governance by sub-committees of the Board of Directors is the third layer, and governance of management process forms the inner most layer.

[9] Ibid

Corporate governance

The corporate governance model of Wipro at the Board of Directors level follows the four-layer framework as shown below:



Our Corporate governannce framework is built on the twin pilars of (i) Robust internal charters that emphasize transparency and integrity and (ii) Objective oversight by independent non-executive directors of the Wipro board. Active participation by the companys shareholders and investors supplements the above process.

Besides its regular functions the Board of directors interacts with the topmost executive body, the Corporate Executive Council (CEC), as well as with the company's senior leadership. The day-to-day management is the responsibility of the management team, which consist of ten business and functional leaders organized as the CEC led by executive chairman. The members of the Council include heads of different Wipro businesses and functional heads of finance, human resources and global delivery. The Board approves the annual comprehensive plan and monitors performance against the approved plan that includes among others, economic, environmental and social aspects of the business[10]. The corporate governance model at Wipro indicates that there are companies which take sustainability as an integrated function within various other functions and within governance model.

[10] Wipro (2008). Sustainability Report, 2007-08

On the other hand ITC has a sustainability committee in place which review, monitor and provide strategic direction to company's sustainability practices towards fulfilling its triple bottom line objectives. This consists of executive as well as non-executive directors of the company. The strategic management of the company rests with the Corporate Management Committee (CMC) comprising full time executive directors and senior management. CMC approves the relevant financial, environmental, occupational health & safety and social policies of ITC. Reports relating to economic, EHS and social performance are provided to the CMC on a monthly basis. In addition to the above, periodic presentations are made to the CMC to ensure performance is in accordance with specified targets[11].

Tata group is an example of how a conglomerate has gone about integrating sustainability initiatives across various group companies. Tata group aims at harmonizing environmental factors by reducing the negative impact of its commercial activities and initiating drives encouraging environment-friendly practices. In one of its many initiatives Tata companies are devising strategies to minimise their carbon footprint. This initiatives started in 2007 with few companies and now being followed by many under its umbrella. Under its Tata code of conduct the group has a clause dedicated on sustainability. All the group companies are signatories to this code.

To ensure that Tata group companies achieved high levels of business excellence the group has institutionalized Tata Business Excellence Model (TBEM). The TBEM provides each company with an outline to help it improve business performance and attain higher levels of efficiency.

While banking sector don't have direct implication on triple-bottom line but "they are in a unique position to channel capital towards a clean development and play a catalytic role in transition towards sustainability" Rana Kapoor, MD & CEO, Yes Bank. Acting on his own words Yes Bank[12] aims at developing innovative business solutions to social and environment problems and for this it follows the approach of "Responsible Banking". The bank offers innovative financial solutions to address a wide spectrum of issues regarding sustainable livelihoods, food security, public health, education and climate change.

The bank also has environment and social policy with the objective to enable the bank to develop processes to recognise, evaluate, and to the highest degree possible, monitor, the environmental and social facets of banking operations and stakeholders[13]. Such diversity of activities under the scope of sustainability is a clear reflection of diversity which exists at the governance structure of the bank. The Board members are healthy mix of group with experience ranging from sectors such as food processing and agriculture to positions in the state governments.

Companies in international arena are also integrating sustainability well in their functions. The Corporate Sustainability Committee of the HSBC Board is responsible for advising the HSBC Board, committees of the Board and executive management on corporate sustainability policies, including environmental, social and ethical issues.[14]

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[11] ITC (2010) Sustainability Report 2009-10

[12] Kapoor, R. Perspective on Responsible Banking. [Online]. Available from: http://www.yesbank.in/pdf/sustainability_compendium_v7_LR.pdf . [Accessed on: 11 February 2011]

[13] Yes Bank. Environment & Social Policy. [Online]. Available from: http://www.yesbank.in/pdf/esp_2010.pdf . [Accessed on: 11 February 2011]

[14] Moffat, A. (2010) 21st Century Corporation: The Ceres Roadmap for Sustainability. Boston

The other most important thing which is a part of sustainability development and its integration with corporate governance is disclosure of information and transparency. Most of the company's Board talk about transparency and accountability. It's better for companies to work on social, economic and environment front but it is best for them to disclose such information to the world. Companies are realising the importance of disclosure and either they are including sustainability data as a part of their annual reports or they are printing separate reports for the same, sometimes adhering to Global Reporting Initiative framework and sometimes not. Infosys, Wipro, Tata, ITC and few other big companies in India are following GRI framework. Adhering to a standard framework make comparisons easier and gives clearer information to the stakeholder.

Disclosure is just one part of transparency. The more companies say about how they are making money, how they are using their resources and the resources of the stakeholders, the more confidence they will generate not just from the shareholders but from the entire range of it's stakeholders.

In one of its projects the CII-ITC Centre of Excellence for Sustainable Development in collaboration with WWF India and the Carbon Disclosure Project (CDP) came out with India CDP report in the year 2009, 2010 and latest one in 2011. Such initiatives allow companies to analyse and work on information which is important not only for stakeholders but also for the company. It channels the company's thought process towards building strategies towards sustainable development.

The government has also taken a bent towards sustainability by proposing guidelines for corporate social responsibility (CSR) in upcoming Companies Bill 2009. The objective of incorporating CSR in the Companies Bill is to guide Indian corporate on the way of doing business which mainstream sustainability in the decision making process and helping inclusive growth. The guidelines will allow Indian corporate to take voluntary initiatives, too. All of this is the initiative of Ministry of Corporate Affairs which is trying to frame a system of corporate governance in terms of people, planet and profit.

These initiatives by the government, industry bodies and companies are signals of what holds in future. It is in the best interest of Indian corporate to work on ways to make each and every function sustainable. If sustainability has to be integrated with corporate governance it needs to seep into each and every function of the company. Only then can the Board and senior management will look at issues of sustainability from business point of view, in terms of risks and opportunities.

There are evidences that sustainability issues are being incorporated into strategy, but they are limited to just a few big names. The pace at which economic, social and environmental issues are creeping up, a pace higher is required for companies to start looking at sustainability from the framework of governance. Only then the companies will be able to overcome such issues and emerge as winners.

Every corporate crisis either national or international is a clear hint to the existing gap. It is time for companies to look at the framework which bridge this gap and provide tools which help the board and management to proactively deal with future crises. The interface framework hints on how the board and the senior management through the structure of corporate governance can integrate the issue of sustainability with the overall objective of the firm. This process will require transparency, better information circulation, and disclosure.

The responsibility of overseeing sustainability should not lie only with the Board. It should be added to functions of management as well. Functions of the board and the management are well known. However, what is important is to converge sustainability within these functions. It is important that the board and the management don't view sustainability as philanthropy but as a reason to improve, sustain, innovate, and adapt. Each business should create its own strategy for success and address the risks and opportunities of participating in the sustainable economy. Sustainability is not a separate discipline rather a subject which should be integrated with strategy, which is likely through a framework.

4

Interface Framework to Embed Sustainability

Companies should take sustainability seriously. Leadership group needs to realise the importance of sustainability. Boards can no more ignore sustainability challenges. On the one hand, they need to understand and respond to changing stakeholder expectations of the role of business. On the other hand, they need to communicate what they consider being realistic expectations of what business can and cannot achieve, and what they consider to be the responsibilities of others.

To achieve this, boards need to engage – both internally and externally – and they need to be transparent in demonstrating the trade-offs they make between competing interests and priorities. For this it is important to understand the elements of the interface that embeds sustainability into corporate governance.

The interface has three elements: board diversity, policy frameworks, and performance evaluation.

Diversify Board

Diversity has many forms including human dimensions (age, skin colour, weight, body shape, etc,) culture dimensions, and skill-set or academic dimension. A company within its functioning includes diverse people taking into consideration the three dimensions mentioned. The stakeholders of the company are also very diverse, be they customers, investors, shareholders, or governments. Thus it becomes very important for the company to have diversity at the leadership levels. Diversity is generally adjudged as the women's representation, which is important but not inclusive.

Significance of board diversity is that it brings in varied experience, multi-layered perspectives and differential understanding. Such diversity makes the board more competent of appreciating sustainability matters and responding with competitive solutions. A diverse board can proactively see the risks arising from any future plan or action of the company and can take corrective action. A diverse leadership within the firm leads to increased competitiveness as great variety of ideas and viewpoints are available.

Diverse board also calls for challenges which arise due to diverse views coming from people with diverse background. However it should be seen as an opportunity because diverse voices can better identify new opportunities, provide a different view point and bring fresh solution and ideas to a discussion.

Steps to Embed

With sustainability being a broad subject its important to understand it from different angles from which it affect the organization and in-turn affect the economy, society and environment. To gauge such an understanding its better to have a mix of board members and senior management who come from backgrounds with different blends. Lack of diversity in our corporate boardrooms is an issue that requires continuing focus. The board members can undertake following steps in order to achieve diversity.

1. Develop diversity policy

A board diversity policy in place specifically laying guidelines for the board will articulate what the organisation wants to achieve and how it will achieve it. In most companies, diversity is an issue relevant to middle and lower levels. At the top, board diversity is mainly gender-based, at best indicative of some representation from employees. In that sense, board diversity is still at nascent stage in India.

A diverse board enhances effectiveness of its actions which increases the productivity and performance of the corporation resulting in increased profitability and shareholder value. Also a diversity enable discussion on topics often not addressed by the board which lessen stagnant thinking, refreshes the organisation, and broadens the perspective of the company.

Not only companies should have a formal diversity policy in place and but also share it with stakeholders through a combination of channels. In 2010 the US Securities and Exchange Commission (SEC) announced a new rule for companies on disclosing to shareholders whether they have diversity policy at the board level and if so, how that policy comes into play when their nominating committees are considering directors.

Again the emphasis should be paid on each and every sub set of diversity. Such a policy in place will not only lead to setting up proper objectives but will further the review of performance against these objectives.

2. Keep track with diversity grid

A diversity grid can be created taking into consideration various subsets of diversity based on demographic and professional indicators. The grid should not only consider categories which are existent to the present board members but also the categories relevant to the skills and knowledge required by the company. It is vital to incorporate sustainability credentials of a candidate being reviewed by the nomination or selection committee. Such a grid will be handy tool for companies to study their boards from diversity angle and also report or disclose the information in response to regulatory or voluntary requirements.

The diversity grid will also help companies clearly identify where the current gaps lie and further strengthen the work of the nomination or selection committee. In order to know how diverse a particular board is, few questions need to be answered:

- Does it bring around the table the necessary skill sets to make the company sustainably resilient and competitive?
- Does it include members familiar with trends relevant to company's areas of business?
- Does it include different races, genders, professional background, industry experience and ethnicity?
- Does it represent stakeholder in some form?

It is important for companies to answer these questions and know where they stand in terms of board diversity. Such an assessment will indicate how diverse a particular board is and also the categories which still remain to be fulfilled.

3. Create selection or nomination committee

In order to place superior talent on the board, a company needs to have a sound and independent recruitment system for appointment and selection of independent directors. Many countries require companies to have a nomination or selection committee for selecting directors. It is time for more companies in India to constitute selection or nomination committee at board level. There are only a handful of companies which view this important. But this may change soon in India. To be in line with international practices, perhaps the new Companies Bill should bring in the provisions of nomination committee on the statute book.

Typically, nomination committee is responsible for leading the search for qualified individuals for election as directors to ensure the board has the right mix of skills, expertise and background. In identifying potential director candidates, the committee and the board also focus on ensuring that the board reflects a diversity of experiences, backgrounds and individuals.

To embed sustainability into board functions, nomination committee could use the diversity grid to identify specific skills sets a candidate could bring to the table. With a sustainability dimension, boards would be composed of a diverse group of leaders with experience at domestic and international levels, as well as experience on other companies' boards, which provides an understanding of different business processes, challenges and strategies that have substantial sustainability bearing.

The selection committee should also take in consideration the various stakeholders of the company while fulfilling the positions because the boards are not just the steering force but also the reflection of our society, economy and environment.

During our research, we came across the following parameter as part of the Board of Directors Nomination Process of the Indian arm of a multinational company in the IT space. It states, "Consideration will also be given to financial management, reporting and control expertise or other experience that would qualify the candidate as a "financial expert" under established standards, and international experience". There is no mention of any new skill-sets that candidates should possess.

Some companies also practice "stockholder recommendations" as part of board of director selection procedure. It may be worthwhile to extend this to "stakeholder recommendations". The initial reaction to this recommendation would be that it will be difficult to reach out to diverse stakeholders, receive and filter recommendations, and most people may not even know what kind of recommendations to put in therefore resulting in junk pile-up. However, the process would remain the same as it is with stockholders, and with technology use it could further be made efficient.

Institutionalise with Policies

It is important to develop policies that cover a comprehensive range of sustainability issues. A corporate policy on sustainability provides specific scope, direction, and expectations underlying sustainable practices. Such policy architecture will facilitate strategy development and deployment for the CEO and board members to keep a tab on sustainability performance, just as they are used to with conventional business performance.

Sustainability in itself is a broad subject and so a sustainable policy should seek to ensure that the company's business management systems and decision-making processes take into account environmental, social and economic issues. The purpose of having these policies is that they will guide the company's action across its various operations, including supply chain, logistics, marketing, product development, design, and employee management[15]. The CEO and the board should ensure that sustainability policy is developed, deployed, and communicated to all stakeholders. They should also review progress on a periodic basis.

Steps to Embed

The arduous task for the board with regards to sustainability is to determine its scope. Another important fact is that a policy developed by one company on sustainability might not hold true for another company because as mentioned before sustainability is a broad subject and includes various angles. Which angle fit right for which company is up to the company to decide. The actionable steps mentioned below can throw light on dealing with such challenges.

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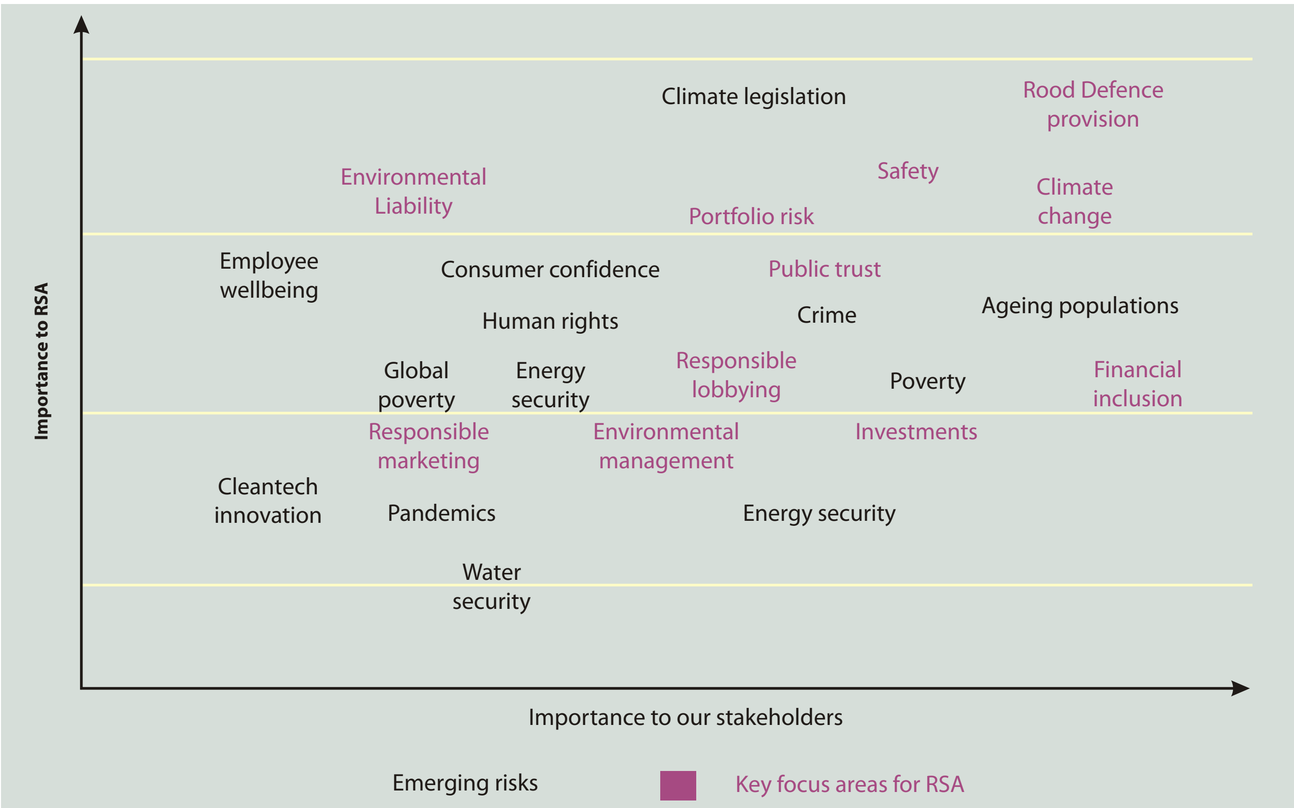
[15] Ibid

1. Identify material issues

It is important that the board knows what are the material issues affecting the organization. Development of policy becomes easier for a company once it recognises the material issues affecting its business and issues which affect the stakeholder. Once the company prioritize these issues it will have the clear understanding of where it stands in terms of its affect on triple bottom line.

Global insurance company RSA is a good example in this case. With the help of UK-based sustainable development organization, Forum for the future, it has developed a materiality assessment matrix. The matrix clearly indicates that issues like environment liability, responsible marketing, environmental management, investments, etc have major influence on the core business of the company. Taking these in consideration the company has policies in key areas such as environment, community and human rights. Overall responsibility of corporate responsibility at RSA lies with the group CEO. The Board routinely discuss corporate responsibility issues affecting the group and conduct an annual review of performance and strategy for the year ahead. An executive level corporate responsibility steering committee oversee implementation of the corporate responsibility strategy and monitors compliance against the global corporate responsibility, environmental, human rights and community policies. The committee meets twice a year and comprises the entire group executive committee to ensure that all top level management are involved.



Source: RSA Corporate Responsibility Report 2009

2. Train and educate

Preparing and drafting a sustainability policy is not a simple task. The process requires professional insights of person/s who can value material issues and can prioritize them in order to develop a policy for them. Any company has numerous material issues and it is not wise to take each one of them into consideration while drafting a policy. For this it is important that proper training is imparted to the board members or a representatives from the board , executive or non-executive members who can be trained on the required skills and can be given the responsibility of drafting the policies. Before implementation the draft can be discussed among board members to get a final approval.

Such a training and education sends a signal to the stakeholders that the board and the organization is committed to sustainability and are willing to dedicate resources to building the capacity of the organization.

Training is also important from the point of view that such policies drafted should address broader socio-economic or environmental issues, such as ILO conventions, UN Global Compact, and other such standards.

3. Filter to business operations

Corporate policies on sustainability should be integrated into the set strictures to make decisions on almost every function of the company sustainable,

- Right from manufacturing to delivery of services,
- Right from employment of employees to their retirements,
- Right from sourcing of raw-material to manufacturing of final products.

Taking in consideration such length and breadth of the business the company should engage in policy on human rights, environment, corruption, and community. It should include labour rights, equality, conservation of environment and its resources, community concerns, corruption, bribery, ethics, etc.

Such a policy on sustainability is an underpinning policy and it provides grounds to not just other offshoot policies but also for sustainability reporting, disclosure, accountability and transparency. All these assume great importance from the investor point of view who are becoming well-aware and demanding about company's initiatives towards triple bottom line.

This implementation should be taken up by the senior management and overseen by the board. The board should question the management from time to time about the status and results of such policies. And thus monitoring of policies is also of utmost importance.

Tata Power has policies on environment, energy conservation, safety & health, HIV AIDS, CSR and e-waste disposal policy. The company also has sustainability council which is headed by the member of Board who is an executive director. This representation creates a link between the leadership of the company and sustainability activities happening within the company.

4. Monitor to measure

Board and senior management should monitor the progress of such policies from time to time on the basis on how well they are integrated into the management systems and operational processes of the organization.

The Board can also set up a council to monitor the progress just like Akzo Nobel. The company's Board of Management has defined and communicated a policy for sustainability, supported by formal directives, regular instructions and constant positive support. It's Board of Management has set up a Council to monitor the sustainability integration process, to embed sustainability in the regular management cycle, to measure progress and to advise the Board of Management on Akzo Nobel's sustainability strategy. The corporate director for sustainability reports to the Board of Management[16].

5. Disclose and report

Stakeholders should be well-aware of company's intention towards sustainability and a clear reflection of this is the corporate policies on sustainability. The organizations should share this information with various stakeholders by putting the policy details on company's website. New entrants to the organization should get well-versed with the policy details by introducing briefs on such policies during their induction process and intranet portal. Shareholders should be given a peek into these policies by giving a separate section in annual report

FMCG giant ITC has policy on human rights with various constituents including policy to ensure respect for human rights policy across the supply chain, policy to prevent discrimination at workplace, policy on freedom of association, policy prohibiting child labour and preventing forced labour from workplace and policy on HIV/AIDS. These constituents are communicated to employees through induction programmes, policy manuals and intranet portals and monitored and audited regularly.

Reporting is important because with changing times stakeholders are becoming more and more demanding and want to see company's goals and priorities on triple-bottom-line.

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[16] Akzo Nobel. (2007). Rigorous and effective Governance Structure [Online] Available from: http://www.annualreport.akzonobel.com/sustainabilityreport2007/managing_sustainability/governance_structure [Accessed on: 1 February 2011]

Recognising the need of embedding sustainability in corporate policies in itself is a big step, but the next big step should be to mainstream it into corporate India. For a company to foray into this domain it is important that it realises the challenges which are material enough for its own business and the challenges which are material enough for the stakeholders. This view will give a company a zoom in view of the risks and opportunities which will arise from ignoring and noticing the triple bottom line issues. It is also important for companies to realise that policy development is not a one time exercise rather it's an on-going process which should be steered by a member of leadership group. The presence of a board member with a preference of independent or non-executive director will give company a chance to look at the same subject from fresh perspective.

Evaluate performance

Of the many lessons learnt from corporate failures in India and worldwide one important lesson learnt is evaluation of board's performance. Within this lesson it is important to embed the issue of sustainability to make it more holistic. Performance evaluation communicates company's priorities by signalling what the management and leadership of the company considers important. The quote "What gets measured gets managed" holds true for the board and senior management.

There are a few companies which link the performance of its employees to sustainability, however there are none which create the same linkage for the board and the senior management. Sparing the leadership group of this link creates a gap between strategy building and execution. The evaluation of employee's performance rests in the hand of management and of management in the hands of board. In the same manner it is important that the due importance is given to the performance evaluation of board. Actual performance outcome provide feedback about the efficacy of a strategy. By defining specific social, environmental and economic work goals for the leadership group and measuring progress towards these targets an organization clearly indicates that triple bottom line performance is an important driver of corporate value.

Steps to Embed

1. Build a strategy-led board

One of the most common plights of Indian corporate board is that it is a compliance driven board and thus it alone considers it is a job done when the company meets the guidelines of the country's security and exchange watch-dog. Thus compliance led boards have little incentive to focus on long-term sustainability issues. To bring the subject of sustainability into the core strategy of a company requires a strategy led board, which uses regulations as a baseline, and go beyond and help influence the company strategy and guide it down the path of sustained value creation.

Achieving such a platform thus calls for a mind-set shift for the board members and senior management. They should take a keen interest in developing a system of evaluation where performance takes in consideration triple bottom line factors. Performance evaluation is critically important because it links performance to the principles of sustainability and aid continuous improvement. The challenge is that at present many existing systems are missing relevant and comprehensive measure of performance.

2. Evaluate self and peers

In some companies self-evaluation at present is undertaken by the board members. However, it is important that the board evaluates itself on sustainability parameters. Self evaluation from board angle is important because board explicitly recognize corporate goals and set specific targets for the company. From sustainability view-point this improves corporate social, environmental and economic performance and focuses attention on areas of concern and priority.

Peer-evaluation gives a 360 degree view of an individual's performance. It is a good process of evaluation because it comes from people occupying similar positions in the organization. At Infosys, for example, the board evaluates the performance of non-executive/independent directors through a peer-evaluation process every year. Each external board member has to present before the entire board on how they have performed/added value to the company. Every board member evaluates each external board member on a scale of 1 to 10 based on the performance indicators.

3. Benchmark

Benchmarking board performance with other organizations board creates an environment of healthy competition. This approach will lead the board members to think about their performance from the organization's stand and not from individual's stand. Thus any gap area if highlighted will be worked upon by all the members of the board and this will create a healthy environment for the organization.

4. Embed criteria in skill matrix

Board can work on developing skill matrix which not only takes into consideration criteria such as board meetings and board discussions but also key performance indicators related to sustainability. This can be linked to the sustainability goals of the organization. It can also reflect stakeholder concerns and suggestions.

Such indicators will be easy to develop for boards once the company becomes aware of the material issues that are important to the company. Developing such indicators will be unique to each company as they will differ according to the sector.

5. Link compensation to performance

One of the fastest ways to gain attention on any initiative is to link it to monetary aspect. Such ideas not only gain attention but also importance. From this perspective evaluating the performance of the board is not just about measuring it against set indicators but also linking their performance to their compensation as well. This can lead to development of innovative compensation schemes with sustainability knitted in the yarn of business.

There are a few companies which are moving on this path, which includes Intel. The company has linked a portion of annual bonus of its employees, right from front-line up through the CEO, on the basis of firm's performance on measure like product energy efficiency, completion of renewable energy and clean energy projects, and the company's reputation for environmental leadership. In 2009 the company also added into the equation performance on reducing the company's carbon footprint. In the same manner Marks & Spencer has outlined executive pay incentives as part of its Plan A Program. Under this program, Marks & Spencer hopes to achieve the ambitious goal of becoming the world's most sustainable retailer by 2015. Compensation for executives is tied to the completion of Plan A goals. Energy giants National Grid and Xcel energy have also integrated sustainability into company's compensation model by linking executive pay to GHG reduction.

Such executive compensation plans and packages should be taken as examples by Indian corporate as well. It is also important to work around the similar innovative schemes for non-executive/independent directors. Being the member of Board they do form a part of decision making process and hence they too should be made accountable towards sustainability issues by embedding triple bottom line in their performance evaluation and compensation package.

Such initiatives by the company should also be disclosed in their corporate reports and should be highlighted on the internet portal in order to make the stakeholders aware of how the leadership council of the company is being evaluated and compensated. Performance evaluation and compensation with implanted sustainability are one of the many forces that will steer the company towards a sustainable organization.

5

Final Remark

India is moving on sustainability and the proof is the examples of Wipro, Infosys, ITC and few other who are doing their bit towards achieving a sustainable future but in their many initiatives and plans what is missing is totality. At present there are only a handful of companies which have taken a serious note about sustainable development. Many still are floating in belief about incomplete definition of sustainability; many don't know how to move ahead on the path of sustainable development. This thought piece aims to bridge the gap for companies about various corporate angles of sustainability, what exactly is sustainability, how important is the role of leadership group to steer the company towards this path, how other companies in India are doing their bit and how just doing bits of sustainability will not take the nation towards a sustainable future.

It is time for corporate India to realise the importance of holistic approach towards sustainability and how future risk can be turned into present opportunities. Solution to these challenges is right in front of us just a wider look and wider depth is required to understand triple bottom line from corporate angle. Board and senior management must realise that gone are the days of business as usual approach. Every new day is now calling of innovation wrapping in sustainability across entire business models.

The sooner this realisation comes in and the sooner companies start acting on these challenges the sooner they will benefit and will in-turn benefit the society, environment and economy. Bits and pieces of sustainability is a solution for short-term, for long-term, sustainability should come across as silhouette of every function; it should not be thought but practised.

It is creditable that this report takes a holistic approach to sustainability, encompassing environment, health, safety, corporate social responsibility, philanthropy and community. Completely agree with the authors that if sustainability has to be integrated with corporate governance it needs to seep into each and every function of the company. Only then can the Board and senior management look at issues of sustainability from a business point of view, in terms of risks and opportunities. At the same time, commitment and sincerity, at the end of the day, holds the key. Even the most thoughtful and well-drafted policies and procedures are destined to fail if directors and management are not committed to enforcing them in practice.

- Sunil Kant Munjal, Chairman, Hero Corporate Service Ltd

With focus shifting to India as one of the growth drivers of world economy in 21st century, Indian corporations have a much wider role to play in world arena. However, with greater opportunity, Indian corporations will also come under tighter scrutiny and the expectation of stakeholders will be higher both in terms of business objective fulfilment and corporate sustainability. I am very hopeful that in times to come some world class corporate governance models will emanate from Indian companies. This report by CII-ITC Centre of Excellence for Sustainable Development is a right step at a very opportune time.

- Thomas Varghese, CEO, Aditya Birla Retail

By managing sustainability related aspects companies can reduce the risk to their performance in the emerging environment where investors are increasingly viewing sustainability related performance of companies as a proxy for management quality.

- Roopa Kudva, Managing Director and CEO, CRISIL Ltd

The CII-ITC Centre of Excellence for Sustainable Development is an institution that creates a conducive, enabling climate for Indian businesses to pursue sustainability goals. It creates awareness, promotes thought leadership and builds capacity to achieve sustainability across a broad spectrum of issues.

A pioneering effort by CII, the Centre is the fountainhead of ideas and practices to promote Sustainability. It enables Indian businesses become sustainable, and channels the potential of Indian industry to power India's agenda for inclusive growth and sustainable development. It enables businesses transform themselves by embedding the concerns of sustainable development into their own strategies and processes.

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Confederation of Indian Industry

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CII has taken up the agenda of "Business for Livelihood" for the year 2011-12. This converges the fundamental themes of spreading growth to disadvantaged sections of society, building skills for meeting emerging economic compulsions, and fostering a climate of good governance. In line with this, CII is placing increased focus on Affirmative Action, Skills Development and Governance during the year.

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