Australian Institute of Company Directors

Elevating stakeholder voices to the board

A guide to effective governance

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Foreword

Debates around shareholder primacy versus stakeholder capitalism cloud a core truth: that any organisation in order to succeed over the long term must consider its external impact, and not simply what is expedient today. An organisation that prioritises short-term outcomes, regardless of harm to others, will erode their customer base, disenfranchise employees and damage the community trust that lies at the heart of any viable business.

Recent high-profile governance failings at Rio Tinto and AMP highlight the damage and community scrutiny that follows when decisions are disconnected from stakeholder interests.

For Australian directors, their duty to act in the best interests of the corporation provides the latitude for complex judgments to be made. Directors can and should consider the reputational impact of their decisions, and have a wide discretion to determine what is in the long-term interests of the corporation. Rightly, Australian courts are reticent to second-guess complex commercial decision making.

This makes it all the more important for directors to carefully consider the inputs, particularly those external to their organisation, required to arrive at well-informed, value-creating decisions. An effective framework for stakeholder governance can play a part in this.

Our guide highlights how Australian directors currently seek to elevate the stakeholder voice in their boardrooms, while suggesting ways in which practice can improve. At the same time, we have spoken with a wide range of stakeholders – representing consumers, workers, suppliers, Aboriginal and Torres Strait Islander peoples, and campaigners - to gain their perspective on what effective stakeholder engagement by organisations, and their boards, entails.

Unsurprisingly the picture painted is a complex one – boards must rely on management to cultivate healthy stakeholder relations, while at the same time knowing that a failure to do so will lead to significant reputational risk. In some cases, stakeholders wish to speak face-to-face with board members in order to directly convey their perspective, unfiltered by management or minders. What is clear is that organisations must have a strategy and that there are many practical steps boards can take to ensure they send clear signals regarding the importance of stakeholders.

It would be naive to suggest that effective stakeholder governance will always lead to sound decisions that enjoy widespread support. Indeed, the essence of a non-executive director role is that we are routinely asked to make complex decisions with imperfect information and with a degree of distance from day-to-day operations.

The AICD is committed to strengthening society through world-class governance and we hope that this guide will assist boards to make better decisions that are consciously informed by the environment and society in which they operate. Community expectations are rising, and it is our challenge to meet them.

On behalf of the AICD, I am grateful to the many people who have contributed to this guide, including the directors and stakeholder representatives interviewed and the input provided by our AICD advisory bodies.

Angus Armour FAICD

Managing Director and Chief Executive Officer, Australian Institute of Company Directors

Purpose and scope of this guide

This document has been developed as a guide for directors to identify and elevate stakeholder voices to the board. The focus of this guide is on non-shareholder stakeholders.

This guide does not attempt to prescribe a fixed set of rules for stakeholder governance; rather, it provides some core principles and steps to guide boards. The guide will:

- summarise the legal duties relevant to stakeholder engagement;
- identify aspects of effective stakeholder governance;
- help directors weigh up the interests of stakeholders when making decisions; and
- provide insights on the hallmarks of good engagement.

Importantly, this guide incorporates advice from Australian stakeholder groups on what successful stakeholder governance looks like from their perspective. In this context, we have engaged organisations that represent key stakeholders including customers, employees, suppliers, Aboriginal and Torres Strait Islander peoples (First Peoples), as well as activists and community groups with perspectives on matters such as climate change, human rights and the environment. We have excluded engagement with government and regulators given the different dynamics at play.

The principles and insights that are presented in this document have been distilled from interviews with experienced directors and stakeholder groups in Australia, as well as subject matter experts and board advisers. We have used case studies where relevant to highlight examples of where boards have demonstrated effective stakeholder engagement.

Executive summary

Stakeholder governance requires organisations to identify, engage with and understand stakeholder perspectives on key issues, and then reflect on how these perspectives should be considered in decision making.

If done well, stakeholder governance strengthens an organisation and will promote its long-term success to and for the benefit of shareholders and stakeholders alike. Poor stakeholder governance, by contrast, will typically increase the organisation's financial and non-financial risk profile and may precipitate major reputational damage.

BOARD'S ROLE IN STAKEHOLDER GOVERNANCE

Broadly, the board is responsible for the overall governance, management and strategic direction of the organisation.

More particularly, directors have duties at law in Australia to act in good faith and the best interests of the organisation. Traditionally, this duty has been understood as owed to shareholders as a whole. It is increasingly recognised, however, that the best interests of an organisation cannot be isolated from the interests of its stakeholders, including employees, customers, suppliers and the community.

Recent Australian court decisions demonstrate that directors have considerable discretion to take into account a broader set of stakeholders when making decisions on behalf of the organisation – indeed, in a practical sense, doing so is often necessary to protect the organisation's reputation and ensure its sustainability over the long term.

This, coupled with heightened community expectations of corporate behaviour, means that organisations are increasingly being asked to look beyond the short-term interests of their shareholders or members. High profile governance failings since the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry highlight the willingness of stakeholder groups and the media to work together and have a voice on issues.

Understanding stakeholder perspectives and how the organisation is managing relationships with key stakeholders is a deliberate exercise, and it is critical for the board to effectively discharge these responsibilities.

In most organisations and circumstances, management should lead day-to-day stakeholder engagement. However, the board should create a culture that puts stakeholders at the centre, ensure it has access to accurate and, where necessary, independent information about stakeholder perspectives and engage with key stakeholders directly, as appropriate. At the heart of this should be organisational openness for two-way dialogue rather than an attempt to "communicate" through tension points. Relationships must be enduring and mutually respectful, rather than ad hoc and transactional.

Management perspective	Director perspective
How does management ensure it understands the needs of key stakeholders and seeks to reconcile them with those of the organisation?	How does the board assess both the board and the organisation's relationships with key stakeholders? What role does the board play in engaging with stakeholders?

A director's role is broader than just sitting around the board table. Directors must create opportunities to engage with community and stakeholders.

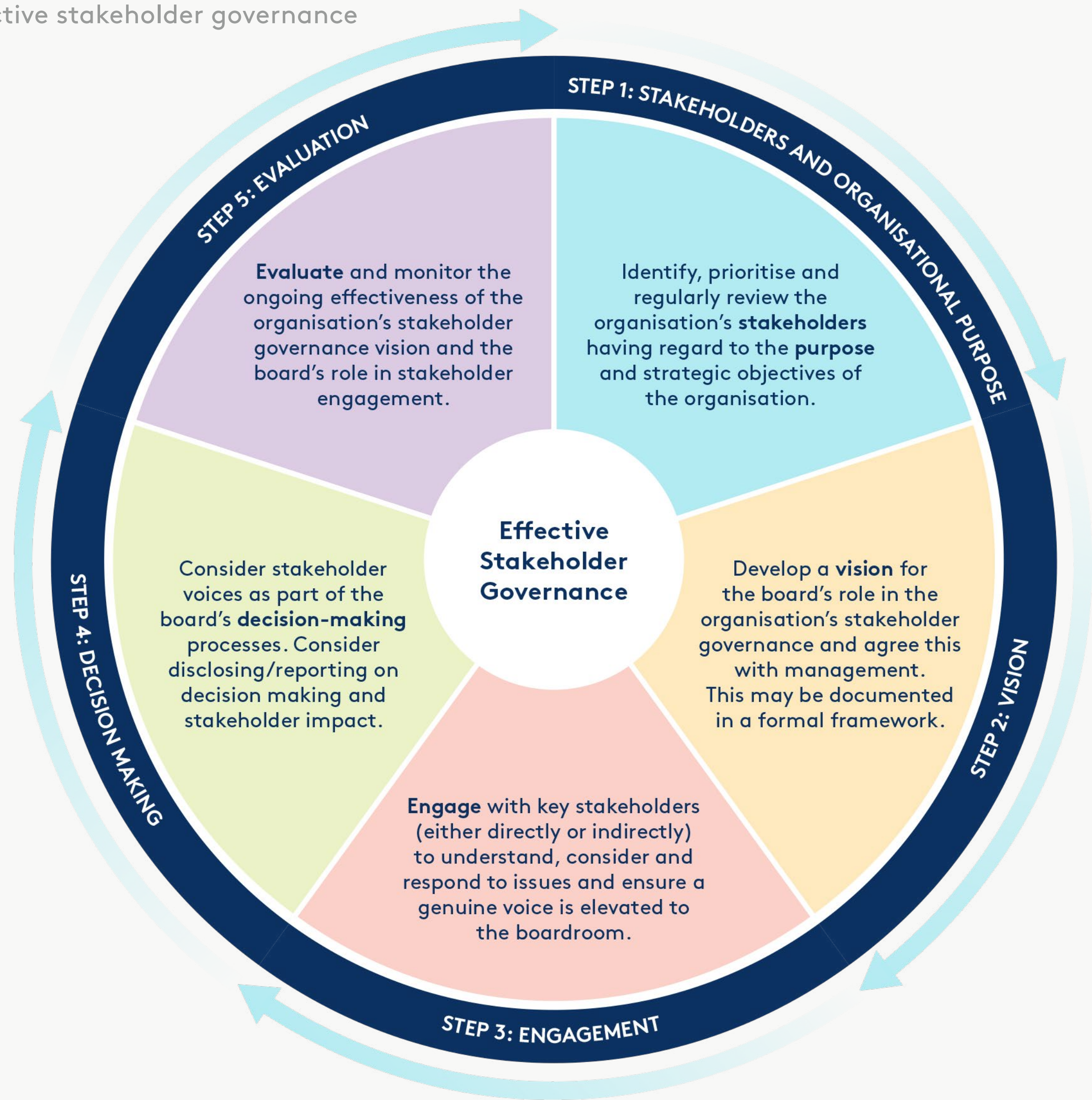
– Shannon Adams FAICD, Chair, World Vision Australia.

There is no 'one size fits all' approach to stakeholder governance. A board's approach will be tailored depending on the purpose, size and nature of the organisation, and type of stakeholders involved. Boards of smaller organisations may not have established a formal framework for stakeholder governance, nor undertaken a deliberate identification exercise. However, even the smallest organisations will have important stakeholder relationships and can benefit from applying some or all of the principles outlined below.

Boards need to ask themselves: How can they make stakeholder engagement a priority? How can they make it meaningful? Do they want to do it better?

– Melinda Cilento, Chief Executive, CEDA; Co-Chair, Reconciliation Australia; Non-Executive Director, Australian Unity.

Fig 1: Effective stakeholder governance



Stakeholder governance steps

STEP 1:
STAKEHOLDERS AND ORGANISATIONAL PURPOSE

Stakeholders are groups that have an interest in an organisation, are likely to affect or be affected by the actions of an organisation, or whose actions can impact the operation or business model.

Investing time in identifying and prioritising stakeholders and assessing their interests forms the basis for effective stakeholder governance.

Identifying and prioritising stakeholders is a dynamic process - stakeholder groups may be in conflict and their priority may evolve over time. The board and management should regularly review the stakeholder map and determine who they consider to be material and relevant stakeholders.

Key questions for the board to ask:

- Which groups are vital to the organisation's long-term success and what are their interests?
- Which stakeholder group(s) are likely impacted (both positively and negatively) by the actions of the organisation?
- Does the organisation need to reassess its key stakeholders? How often should this be done?

STEP 2:
VISION

Boards should consider overseeing the development and adoption of a formal framework to guide the company's stakeholder engagement activities. This will identify why stakeholder governance is important and ensure that the board considers stakeholder perspectives in its decision making and other governance processes.

SMEs and NFPs may not need a formal framework but should be asking themselves these questions.

Key questions for the board to ask:

- Does our organisation need a formal stakeholder governance framework?
- Do existing governance frameworks ensure the board's information needs are met in relation to stakeholder perspectives for its decision making, oversight of management, and risk management?
- Does the board's vision for stakeholder governance connect to the organisation's values?
- Is it clear who is responsible for engaging with each stakeholder group and when?

Stakeholder governance steps (cont)

STEP 3:
ENGAGEMENT

The majority of stakeholder engagement occurs at the management level. To provide effective oversight of management, the board must ensure it is receiving timely and accurate information about stakeholders.

There may be circumstances where the board determines that it should engage directly with stakeholders. The frequency of such direct engagement will vary from stakeholder group to stakeholder group and issue to issue. Refer to **page 22** for an overview of the types and frequency of engagement.

The board must consider what form of engagement is most appropriate for the stakeholder group, not just the board.

Key questions for the board to ask:

- Should the board be directly involved in engagement with a particular stakeholder group or on a particular issue?
- Is the board's engagement with each stakeholder commensurate with their importance?
- Has the board considered whether the form of engagement with a particular stakeholder is tailored to that group?

STEP 4:
DECISION MAKING

Boards will derive the greatest value from their stakeholder engagement by using that information to inform decision making.

The board can take practical steps to ensure sufficient consideration is given to stakeholder perspectives, including requesting that board papers address stakeholder perspectives and impact, schedule meetings with stakeholders as part of regular board meetings or strategy days and delegate responsibility for understanding specific stakeholders/issues to board or advisory committees.

The board should also consider if it is necessary to communicate decisions with an impacted stakeholder group and how best to do so.

Key questions for the board to ask:

- How does the board's decision-making process reflect stakeholder perspectives?
- Is the board getting the right information about stakeholders (for example, do board papers consider the 'stakeholder impact') and does it allocate sufficient time to consider these issues?
- Does the board have the right structures to enable a deep dive on key stakeholders and/or issues (for example, would an advisory committee support decision-making processes or does the board have a board committee that explicitly encapsulates stakeholder impact in its remit)?
- How should the board report on and/or communicate decisions to impacted stakeholders?

Stakeholder governance steps (cont)

STEP 5:
EVALUATION

It is important to assess the effectiveness of the organisation's stakeholder governance and adjust as necessary.

This should be led by management with board oversight. Directors may consider commissioning an external party to undertake an evaluation of the health of stakeholder relations.

Key questions for the board to ask:

- Does the board regularly review the effectiveness of the organisation's stakeholder governance vision/strategy?
- What independent, external data speaks to the organisation's relations and stakeholder impact?
- Should the board engage an external party to assess the state of our stakeholder relations?

BOARD COMPOSITION CAN ALSO SUPPORT EFFECTIVE STAKEHOLDER GOVERNANCE

A board should be made up of directors that have broad experience and understand the role of directors. The board could consider whether a board member who understands a particular stakeholder would be a good addition to boardroom discussion if they feel, for example, that a particular stakeholder perspective has been overlooked historically. The board may also wish to consider identifying particular stakeholder expertise in an organisation's skills matrix.

Having an extensive induction process that incorporates education on key stakeholders is also critical (this could include site visits or briefings on the organisation's impact on the community). Ongoing education on particular stakeholder issues is also necessary.

> Directors do not have to agree with the views of stakeholders being put forward. It is not a black and white exercise. Directors need to simply inject themselves into the issues being raised and thoroughly consider and think them through.

– David Gonski AC FAICD*Life*, Former Chair, Australia and New Zealand Banking Group; Director, Sydney Airport Corporation; Chancellor, University of New South Wales; President, Art Gallery of NSW Trust.

HALLMARKS OF GOOD STAKEHOLDER GOVERNANCE

Representatives from diverse stakeholder groups have shared insights on the hallmarks of meaningful engagement and how boards can engage with the individuals they represent more effectively. Key observations include:

DIRECTORS SHOULD UNDERTAKE PURPOSEFUL INQUIRY INTO THE BROADER ENVIRONMENT IN WHICH THE COMPANY OPERATES.

There is no one size fits all approach to effective stakeholder governance. However, a common thread is that successful boards have curious directors who take a genuine interest in the various facets of the environment in which the organisation operates. Through their purposeful inquiry into the perspectives of the company's employees, suppliers, customers and other stakeholders, curious directors are invariably better placed to make informed decisions about the long-term future of the organisation.

Directors that demonstrate an aptitude for stakeholder relations also understand their own prejudices. We heard clearly that it is critical that directors do not think they understand an issue based on their life outside the boardroom. When a director has an awareness of their own motivations, biases and moral preferences they can bring a greater understanding to the board table, which in turn results in better decision making.

> For too long corporations have existed in a bubble, disconnected from other stakeholders, including Indigenous Australians. Organisations can no longer operate in this bubble. They must be informed and clear about their responsibilities.
>
> –June Oscar AO, Aboriginal and Torres Strait Islander Social Justice Commissioner, Australian Human Rights Commission.

BOARDS SHOULD LOOK FOR WAYS TO BUILD AUTHENTIC AND SUSTAINED ENGAGEMENT WITH STAKEHOLDERS, AND MAKE IT EASY FOR THEM TO ENGAGE.

Boards should aspire to build open and respectful relationships with stakeholders, having regard to the following principles:

- **Engagement should be respectful.** The board should acknowledge the expertise, perspective and needs of stakeholders, and enter engagement with an open mindset.
- **Engagement should be enduring and timely.** Engagement with key stakeholders should be continuous and ongoing. An organisation should not make the mistake of engaging with a relevant stakeholder only when it wants/needs something.
- **Engagement should involve recognising that there are discrepancies in power and capability between an organisation and a stakeholder group.** In designing its stakeholder interactions, the board should have regard to cultural, geographic, mobility and language barriers or power imbalances that may constrain effective engagement. This may involve consulting with stakeholders on the most effective ways to address barriers and support effective engagement.
- **Engagement should be transparent.** If stakeholders have given their time, organisations should follow through on next steps. This should include reporting back on the outcomes of stakeholder engagement processes.

STAKEHOLDER CONSIDERATIONS SHOULD BE EMBEDDED IN AN ORGANISATION'S STRATEGY.

As consumers and society increasingly expect more from business, stakeholder governance cannot simply be a risk management or public affairs exercise, but rather be embedded in an organisation's strategy.

Boards must take steps to ensure they have the best possible information (including stakeholder perspectives) to inform the development of the strategy. Strategic decisions will range in scale and scope and may include decisions to enter a new market or withdraw a long-standing product, for example. In making such decisions, the board will need to have regard to the impact entering a new market will have on the local community or how the withdrawal of a product will affect customers.

ADAPTING THE BOARD'S ENGAGEMENT TO THE STAKEHOLDER

The AICD asked representatives from diverse stakeholder groups for guidance on the steps that directors should be taking to elevate stakeholder voices to the board. These representatives highlighted that boards need to design their stakeholder engagement programs around the interests and needs of each stakeholder group, rather than adopt a standardised approach.[1]

CUSTOMERS

Boards must understand the limitations of customer experience metrics. Taking steps to understand the worst experience customers have via qualitative data may help boards uncover hidden issues.

Boards may gain valuable insights through direct engagement with customers. It can humanise the challenges that some customers may face and reconnects the board with the organisation's purpose.

Customer engagement at the board level often includes customer advisory committees, briefings with customer advocates/advocacy groups and starting a board meeting with a 'customer moment'.

EMPLOYEES

Boards often have greater opportunities for engaging directly with employees than other stakeholder groups.

Directors should make the most of this access, particularly to get their own lens on culture. Employees can be a conduit to understand the needs of other stakeholder groups such as consumers, suppliers and the broader community. Most fundamentally they may be able to alert boards to latent risks well before senior management is aware of them.

Types of employee engagement include 'town hall' meetings, site visits, inviting employees at various levels to meet with directors and workforce advisory committees.

SUPPLIERS

Respectful relationships with suppliers can have a significant impact on an organisation's profitability over the longer-term.

Boards should remain alive to the significant power imbalances between big business and small suppliers, particularly around unfair contract terms and payment terms.

Boards should set expectations for reporting and probe management on supplier complaints and outstanding payables.

FIRST PEOPLES

Boards should ensure an organisation fosters genuine, ongoing connections with First Peoples, mindful of the historical actions of their organisation and broader injustices suffered by Aboriginal and Torres Strait Islander peoples.

Where possible, the board should engage with leaders 'on Country' and minders should be left behind.

Boards should be ready for raw and direct feedback.

First Peoples advocates suggest organisations have regard to the UN Declaration on the Rights of Indigenous People, which calls for free, prior and informed consent.

ESG ISSUES

The board should ensure the organisation has taken steps to understand if human rights risks exist in the organisation or its supply chain. Similarly, the board should ensure that environmental issues are given serious consideration. Management should be empowered and resourced to do this work.

Consultations with communities or 'rights-holders' should consider language, cultural and other potential barriers to effective engagement.

Engagement should take place early in any decision-making process.

COMMUNITY

Community encompasses a wide range of stakeholders, ranging from local charities and community groups to local business and government authorities, as well as communities of interest.

The board should remember that engaging with this vast group of stakeholders can improve an organisation's decision making, reputation and competitiveness.

Boards should bear in mind that the community may have a sceptical view of the organisation and efforts to engage with them may be dismissed as disingenuous public relations.

1 Appendix one **(page 31)** explores each of these stakeholder perspectives in further detail, including a number of case studies.

Benefits of stakeholder governance at board level

It is no secret that organisations that are effective at stakeholder governance, are more effective operationally.[2] Maintaining a clear and consistent dialogue with stakeholders, better equips organisations to understand the external environment in which they operate, build goodwill, make informed decisions and ultimately, enhance performance.

ACCOUNTABILITY

Boards taking the lead on engagement can send important signals not only to external audiences, but also internally to all levels of organisations about the values and behaviours it expects to see employees demonstrate when interacting with stakeholders.

DRIVING CULTURE

By demonstrating strong stakeholder governance, the board sets the ‘tone from the top’ and is able to develop an organisational culture that genuinely values stakeholders.

REDUCE COSTS AND CREATE VALUE

While addressing stakeholder concerns can, at times, involve additional costs, over the longer-term these costs may be offset in other ways. For example, a quicker elimination of roadblocks, lower compliance costs, as well as a platform for product and service improvement and innovation.

EFFECTIVE DECISION MAKING

Stakeholder feedback can have a profound impact on a board’s decision making and even mandate a re-think of the organisation’s strategy. As a by-product, management can have confidence that the board is equipped with the right information to make decisions effectively.

> Anything that broadens the horizon of directors to understand the context in which the organisation operates is valuable.
>
> – Gerard Brody, CEO, Consumer Action Law Centre.

MUTUAL TRUST

Engaging with stakeholders not only humanises the board in its collective, but also helps to engender a sense of mutual trust and respect. Over the longer-term, this can improve an organisation’s reputation and standing in society more broadly.

RISK MANAGEMENT

Being alive to the changing expectations of stakeholders can provide directors a broader view of potential internal and external risks. Not to mention, an opportunity to reduce any vulnerabilities with the benefit of those outside perspectives.

SHARED LEARNING OPPORTUNITIES

Stakeholder engagement creates opportunities for two-way knowledge sharing. For boards, it can provide the ultimate temperature check on how the organisation is perceived and its stakeholders’ needs. For stakeholders, it provides an opportunity for a more contextualised understanding of the organisation.

2 J Pfeffer, 2009, “Shareholders first? Not so fast”, Harvard Business Review, July-August, **https://hbr.org/2009/07/shareholders-first-not-so-fast**, (accessed 23 March 2021).

Elevating the stakeholder voice to the board

THE BOARD'S ROLE IN STAKEHOLDER GOVERNANCE

The board is responsible for the overall governance and strategic direction of the organisation.

Understanding stakeholder perspectives and managing relationships with key stakeholders is critical for the board to discharge these responsibilities. Making well-informed high-quality decisions requires the board to understand and balance complex stakeholder interests while ensuring the delivery of corporate objectives. Effective management of non-financial risks such as reputational risk will also require the consideration of different stakeholder perspectives.

It is important for directors to agree upfront with management the rules of engagement, which clearly delineate between the roles of the board and management in stakeholder governance. Day-to-day stakeholder engagement should be led by management. The board will take a more limited role in overseeing management and establishing organisational processes that integrate stakeholder governance into the organisation's broader governance structures and processes.

> Management should own and manage critical relationships with stakeholders. However, there may be circumstances where the board needs to get involved. For example, where there is serious reputational risk it is important for the board to be visible.
>
> – Graham Bradley AM FAICD, Chair, EnergyAustralia, United Malt Group and Infrastructure NSW.

The board must also consider how it develops a culture that genuinely values stakeholders. In this regard, the board has an important role in setting the tone from the top through their individual and collective behaviour.

In doing so, the board needs to consider how it will access accurate and timely information about stakeholder perspectives and ensure that information is not overly 'curated' by management. The Australian Prudential Regulation Authority emphasised the importance of boards challenging management in its 2018 Final Report of the Prudential Inquiry of the Commonwealth Bank of Australia. Stakeholder relations is no different. To that end, where possible, boards should seek out independent external sources of information by which they can test management reporting and assurances.

Nevertheless, there will be situations where boards should engage directly with the organisation's key stakeholders. This should not usurp the role of management but rather reinforce the relationships that management have been building or enable directors to obtain a direct account of a stakeholder perspective. During a crisis (for instance, the COVID-19 pandemic) the board may take a more hands on role in day-to-day management including stakeholder engagement, particularly in smaller NFPs or SMEs where management lack the bandwidth or expertise to do so.

> Our board [Woodside Petroleum] undertakes regular site visits to look at operations and as part of this engagement the board ensures it makes time to speak with Indigenous leaders. We do not consider this to be usurping the role of management, but rather reinforcing the relationships that management has been building.
>
> – Richard Goyder AO FAICD, Chair, Qantas, Woodside Petroleum, AFL Commission.

We explore the time and place for direct board-stakeholder engagement on **pages 19** to **22** below.

Management perspective	Director perspective
How does management ensure it understands the needs of key stakeholders and seeks to reconcile them with those of the organisation?	How does the board assess the organisation's relationships with key stakeholders? What role does the board play in engaging with stakeholders?

The role of the chair

The chair plays a vital role in stakeholder governance. Critically, the chair is responsible for communicating the views of the board, in conjunction with the CEO, to the organisation's shareholders/members, broader stakeholders and the public.

The chair may lead engagement with, or make themselves available to, key stakeholders where necessary. For example, the chair may have one-on-one meetings with key stakeholders or in certain organisations the chair may let employees know that he/she is open to hearing from employees. In addition, the chair should be considering:

- if the board is receiving appropriate information about stakeholders;
- if sufficient time is allocated to considering stakeholder perspectives in decision making; and
- the adequacy of director education and awareness around emerging stakeholder issues.

BOARD COMPOSITION, DIVERSITY AND TRAINING

Selection criteria for non-executive directors

A key responsibility of the board (sometimes delegated to the people and nominations committee in larger organisations) is to assess its own composition and determine whether it has the right balance of directors to understand the organisation's long-term interests and the environment in which it operates. Boards with a diverse mix of career and life experiences are less likely to succumb to groupthink and have been shown to contribute to improved performance and promote a better understanding of an organisation's stakeholders.[3]

One approach to acquiring stakeholder expertise in the boardroom is to appoint board members with a deeper understanding of a particular stakeholder group. Such a director can then reflect this perspective at the board table. The board may wish to consider identifying particular stakeholder expertise as a core component of an organisation's 'skills matrix' and reflecting this in the search and selection criteria for new non-executive directors.

3 L Fink, 2018, Letter to CEOs, 12 January, **https://assets.documentcloud.org/documents/4350914/BlackRock-s-Laurence-Fink-Urges-C-E-O-s-to-Focus.pdf**, (accessed 23 March 2021); S J Creary, M McDonnell, S Ghai, and J Scruggs, 2019, "When and Why Diversity Improves Your Board's Performance", Harvard Business Review, March 27, **https://hbr.org/2019/03/when-and-why-diversity-improves-your-boards-performance**, (accessed 23 March 2021); S Singh and K McDonald, 2018, "Does Diversity Provide a Profitability Moat?", AXA Investment Managers, June, **https://www.axa-im.com/documents/23818/206774/180808+Rosenberg+equities+Does+diversity+provide+a+profitability+moat#:~:text=We%20find%20evidence%20that%20diversity%20on%20the%20board%20can%20create,the%20face%20of%20competitive%20pressures**, (accessed 23 March 2021).

Stakeholder representatives on the board

In some cases, although uncommon for public companies in Australia, an organisation may determine to formally appoint a stakeholder representative to the board as a director. This may be facilitated by reserving or requiring a board position be appointed from a particular stakeholder group, such as an employee-elected director or, in an NFP context, a beneficiary of the organisation's services. For example, ACON, a leading HIV prevention organisation, constitutionally mandates that a person with an HIV seropositive status sits on the ACON board. The President of ACON Justin Koonin FAICD comments that "having stakeholders on the board is a valuable way to ensure stakeholder input on every board decision".

Worker representatives

In Australia, unique to the superannuation sector, funds often have employer and employee-representative directors. Internationally, company boards in countries such as Germany, Norway, Sweden have long had worker representatives.

The UK government has recently increased the focus for listed company boards on understanding the interests of employees. Under the revised UK Corporate Governance Code (effective January 1, 2019), UK companies can choose one of three options to give employees a formal voice in the boardroom. This can be an employee-elected board member, workforce advisory board or the designation of a non-executive director to engage with employees.

In Australia, the ALP's 2019 federal election platform stated that it would "… examine measures that increase collaboration between employers and workers, including worker representation on boards, giving consideration to global models currently in operation".

Daniel Walton, National Secretary of the Australian Workers Union, believes "employee representatives on boards could do more than identify labour-related risks. They would help transform company/ employee collaboration and innovation."

In an Australian context, traditionally, efforts to appoint worker representatives to boards have been resisted as directors are required to act in the bests interests of the company rather than any specific stakeholder.

Board induction and ongoing development

A well-functioning board should have an induction process for new directors including briefings about important stakeholders and how those stakeholders inform the purpose and strategy of the organisation.

The induction process could involve meetings with key stakeholders and their representatives, site visits, and management and external briefings on the organisation's impact on the broader community.

> New directors should be onboarded and educated about stakeholder engagement. It is important for them to engage with external parties to get an unfiltered perspective on issues.
>
> – Alix Pearce, Campaigns Director, The Climate Council.

Key questions the board should be asking about board composition and training:

- Should the board incorporate 'stakeholder expertise' into its board skills matrix?
- Would the board benefit from a stakeholder representative?
- Does the board provide appropriate information about the organisation's stakeholders during board induction?

EFFECTIVE STAKEHOLDER GOVERNANCE

There is no 'one size fits all' approach to stakeholder governance. A board's approach will obviously be tailored depending on the purpose, size and nature of the organisation, and type of stakeholders involved. Boards of smaller organisations may not have established a formal framework for stakeholder governance, nor undertaken a deliberate identification exercise. However, even the smallest organisations will have important stakeholder relationships and can benefit from applying the principles outlined below.

What follows are some key principles that can guide boards on effective stakeholder governance and oversight. In some cases, these principles may be more iterative, requiring the board to continually reflect on additional stakeholders or perspectives.

The board should:

1. Identify, prioritise and regularly review the organisations' stakeholders having regard to the purpose and strategic objectives of the organisation.
2. Develop a vision for the board's role in the organisation's stakeholder governance and agree this with management. This may be documented in a formal framework and should have linkage with the organisation's broader strategy.
3. Engage with key stakeholders (either directly or indirectly) to understand, consider and respond to issues and ensure a genuine voice is elevated to the board.
4. Consider stakeholder voices as part of the board's decision-making processes. Consider disclosing/reporting on decision making and stakeholder impact.
5. Evaluate and monitor the ongoing effectiveness of the organisation's stakeholder governance framework and the board's role in stakeholder engagement.

Each of these steps is explored in further detail below.

STAKEHOLDERS AND ORGANISATIONAL PURPOSE

Identify, prioritise and regularly review the organisation's stakeholders having regard to the purpose and strategic objectives of the organisation.

Stakeholders are groups that have an interest in an organisation, are likely to be affected by the actions of an organisation, or whose actions can impact the operation or business model. Investing time in identifying and prioritising stakeholders and assessing their interests provides a strong basis from which to build effective stakeholder relations and achieve better outcomes for the organisation.

Most organisations will consider its workforce, customers, suppliers and shareholders/members to be key stakeholders. We would expect communities in which the organisation operates to also feature on the list, for example First Peoples and local communities in which an organisation operates. It is also important to consider stakeholders who may not be currently accessing your organisation's services or products. This might include people with disability and people from culturally and linguistically diverse backgrounds and communities.

Importantly, boards should recognise that stakeholders are not siloed groups, and that there can be considerable shared or competing interests. Cross-collaboration and multi-faceted engagement is sometimes warranted on certain issues. For example, First Peoples and local communities may have converging interests and concerns that are shared with activist groups relating to human rights and environmental issues. Conversely there may be times where local communities may support a project for its potential to generate employment whereas outside groups may oppose due to its potential environmental impact.

Even though shareholders are beyond the scope of this document, a clear message that emerged during interviews is that stakeholders are increasingly engaging directly with investors, particularly regarding ESG matters. Directors should be alive to the role investors play in championing stakeholder perspectives.

Stakeholder mapping

Boards, together with management, should identify the groups which influence the organisation's operations or could be affected by the organisation's operations. This task is often referred to as 'stakeholder mapping'. When undertaking stakeholder mapping, the board needs to keep in mind:

- groups that are vital to the value of the organisation in the long-term;
- groups which are likely impacted (both positively and negatively) by the actions of the organisation; and
- groups whose behaviour and actions can impact the operation or business of the organisation.

This requires consideration of the purpose and strategic objectives of the organisation, and often, consideration of those groups that may be indirect stakeholders yet have a significant impact on the organisation. These are sometimes referred to as 'influencers' and could include activist groups.

In most cases, stakeholder mapping will be undertaken by management. Nonetheless, it is incumbent on the board to have input, reviewing and reflecting on the stakeholder map to ensure all key stakeholders and their interests have been identified.

NFP stakeholders will, of course, be different to those of for-profit organisations. Naturally, the most important stakeholders for a NFP will be the people that the organisation exists to benefit. Other stakeholders may include, members, clients and their families, volunteers, donors, funders, staff, government, general public, and carers.

It is important that NFPs do not fall into the trap of thinking that just because they do not exist to provide a commercial return to shareholders that they cannot cause considerable harm to stakeholders. The Child Sexual Abuse Royal Commission was a stark reminder that many NFPs have caused considerable harm to those that they were charged with caring for and protecting.

Prioritising stakeholders

Once stakeholders have been identified, they should be prioritised to determine their importance to the organisation. This may involve the board asking the following questions:

- Which stakeholders are most critical to the organisation's operating environment and/or long-term success?
- What are the organisation's current priorities and how do these impact stakeholders?
- Are there current issues that impact stakeholders which require immediate board attention?

Reviewing the 'stakeholder map'

Identifying and prioritising stakeholders is a dynamic process. Stakeholders groups and their priorities may evolve over time. Organisational strategy, requirements of the business or regulatory changes may also impact the stakeholder mix. Consequently, it is important for the board and management to review the stakeholder map regularly and recalibrate as necessary.

Key questions to identify and prioritise stakeholders:

- Which groups are vital to the organisation's long-term success and what are their interests?
- Which stakeholder group(s) are likely impacted (both positively and negatively) by the actions of the organisation?
- Does the organisation need to reassess its key stakeholders? How often should this be done?

VISION

Develop a vision for the board's role in the organisation's stakeholder governance and agree this with management. This may be documented in a formal framework.

Boards should consider overseeing the development and adoption of a formal framework to guide the company's stakeholder engagement activities. The ultimate objective of such a framework is to both identify why stakeholder governance is important to the organisation and ensure that the board can incorporate stakeholder perspectives into its decision-making, governance processes and overall strategy.

The framework should ensure that day-to-day stakeholder engagement remains principally the role of management and the board does not assume management's responsibilities. Further, the framework should communicate to management that stakeholder governance and impact is a core organisational value, critical to the organisations' strategy and long-term value creation.

> It is important that boards manage stakeholder engagement to be confident the board is hearing 'representative' feedback; not anecdotal or feedback limited to the 'loudest voice'.
>
> – Dr Katrena Stephenson GAICD, Director, Environment, Development and Community at Kingborough Council.

A well-designed stakeholder governance framework for many organisations will address topics such as:

- Why stakeholder engagement is important for the organisation;
- The vision for stakeholder governance and its connection to the organisation's values;
- The board's information needs in relation to stakeholder perspectives for its decision making, oversight of management, and risk management;
- Resourcing and responsibility for engagement activities, including the roles of the board, senior management and business units;
- Internal policies and procedures documenting effective stakeholder engagement processes, including opportunities to provide stakeholders with feedback as necessary;
- Key performance indicators (KPIs) for stakeholder engagement and satisfaction, a primary mechanism for the board to create accountability.

Of course, it is important that each organisation tailors its stakeholder governance framework to its circumstances, including the type and number of the organisation's key stakeholders, as well as its resources, purpose and culture. It may be unnecessary for boards of smaller organisations to establish such a framework. However, directors of such organisations should turn their minds to some of the topics outlined above to promote effective stakeholder governance.

Key questions for the board to ask regarding a stakeholder governance framework:

- Does our organisation need a formal stakeholder governance framework? Do existing governance frameworks ensure the board's information needs are met in relation to stakeholder perspectives for its decision making, oversight of management, and risk management?
- Does the board's vision for stakeholder governance connect to the organisation's values?
- Is it clear who is responsible for engaging with each stakeholder group and when?
- Are stakeholder KPIs necessary to promote effective stakeholder engagement by management?

ENGAGEMENT

Engage with key stakeholders (either directly or indirectly) to understand, consider and respond to issues and ensure their voice is elevated to the board.

Form of engagement

Board roles and responsibilities are considerable, and it is neither possible nor desirable for a board or individual directors to engage directly with all stakeholders.

The majority of stakeholder engagement occurs at the management level where there is daily engagement with stakeholders such as employees, customers and suppliers.

To provide effective oversight of management, the board must set clear expectations to ensure management is providing timely and accurate information about stakeholders to the board. This information should be included in board papers and may take the form of reports, metrics and assessments on stakeholder perspectives.

> A good director has to have a high degree of scepticism about the information presented to the board and the courage to ask probing questions of management if they have concerns.
>
> – Graham Bradley AM FAICD, Chair, EnergyAustralia, United Malt Group and Infrastructure NSW.

However, directors need to be alive to the limitations of quantitative data that can hide important challenges faced by particular subset of stakeholders such as vulnerable customers.

According to Alan Kirkland, CEO, CHOICE, "the average isn't your friend. A deep dive on particular complaints is necessary to flush out systemic issues."

To overcome this, boards should consider requesting information from management about purportedly 'outlier' cases, as well as qualitative data such as verbatim customer and employee feedback.

Further resources: Culture

The AICD and Australian Council of Superannuation Investors (ACSI) joint research report, **Governing Company Culture: Insights from Australian Directors**, reminds boards to be careful about how they use and interpret reported metrics. Raw numbers can be misleading, so boards should interrogate and triangulate data to get a full picture and look at trends over time which may be more indicative of certain behaviours in the workplace. For example, a high attrition rate may suggest an underlying cultural problem in certain pockets of the organisation. In relation to employee surveys, respondents may not always answer questions in the intended way if they believe their responses are not anonymous (even if told otherwise).

At the same time, effective stakeholder engagement can require direct engagement by the board – with frequency determined according to need. This may be regarding ad hoc issues (such as managing an acute challenge or risk) or because the board seeks an unfiltered stakeholder perspective, for example to inform strategic planning. Similarly, there will be stakeholder groups like First Nations traditional owners that expect peer-to-peer, board-to-board engagement to maintain an open and respectful relationship.

CASE STUDY:
Collins Foods Limited

Collins Foods Limited, the largest franchisee of KFC stores across Australia employs more than 10,000 teenagers at its outlets. At the height of COVID-19, different sets of social distancing rules applied across the states and territories, causing significant disruption to how in-store dining and takeaway at KFC stores could be managed from both a staffing and food safety perspective. Chair Robert Kaye led a direct communication campaign, calling close to 200 employees randomly selected from different levels within the company to check on how the new protocols were being received, check on frontline employees' wellbeing and, most importantly, learn what practical and moral support the organisation could provide.

This was an incredibly effective way to take the pulse at all layers of the organisation and gain a sense of what was happening on the ground without it being sanitised.

– Christine Holman GAICD, Director, CSR Limited, Metcash Limited, Collins Foods Limited, Blackmores Limited, The Moorebank Intermodal Company, The McGrath Foundation, The Bradman Foundation, The State Library of New South Wales Foundation and The ICC T20 World Cup 2020/2022.

In some circumstances, it may be beneficial for an external party to facilitate stakeholder interaction. Refer to the 'Day in the Life' example on **page 32** for an example of where Financial Counselling Australia has facilitated this form of engagement in the financial services sector.

Good practice requires that board members be given the opportunity to observe customer engagement or 'walk the factory floor'.

– Gerard Brody, CEO, Consumer Action Law Centre.

The board should play a direct or more active role where visible board engagement clearly adds value to the stakeholders or where risk mitigation is critical for the organisation.

– Kathleen Conlon FAICD, Chair, Lynas; Director, Bluescope Steel, The Benevolent Society, REA Group Limited and Aristocrat Leisure Limited.

Where the board is engaging directly with a stakeholder group, the board must be alive to, and consider, what form of engagement is most effective and convenient for the stakeholder group, not just the board.

Boards should be mindful that stakeholders may not be aware of the full range of interests that the board is grappling with, nor appreciate that their interest is just one input. OZ Minerals stakeholder day (discussed below) enables stakeholders to understand the sometimes competing views of others.

There should be sensitivity around stakeholder engagement and how it can be facilitated. It must be considered and thoughtful, not just applying a process that works in a corporate environment.

– Amy Sinclair GAICD, Regional Representative for Australia, New Zealand and the Pacific, Business & Human Rights Resource Centre.

Directors can also undertake stakeholder monitoring, as well as ad hoc media and internet tracking. A number of directors interviewed regularly review GlassDoor (a website where employees can anonymously review their employer), Zammer, Seek and similar websites to get direct feedback from current and former employees that has not been sanitised by management. Similarly, an organisation's LinkedIn, Twitter and Facebook accounts will also have unfiltered customer feedback. Some of the comments may be spurious or unfair, but some issues may be identified that warrant the director asking further questions of management.

Stakeholder days are another useful mechanism to provide an opportunity for stakeholders to meet and interact. As mentioned by Daniel Walton, National Secretary of the Australian Workers Union, "boards are very good at holding investor days which provide unencumbered access to directors, but other than the annual general meeting, you don't often see an opportunity for this type of consultation or exposure to the board for other stakeholders".

CASE STUDY:
OZ Minerals

OZ Minerals defines its strategy around five stakeholder groups: Shareholders, Suppliers, Staff, Government and Community. All decisions and KPIs are assessed against value creation for these five stakeholders.

To ensure all stakeholders have an opportunity to meet and interact, OZ Minerals holds an annual stakeholder day in which it brings together 300 people representing all stakeholders to their premises in Adelaide. According to Rebecca McGrath FAICD, Chair, OZ Minerals Ltd, "the stakeholder day allows OZ Minerals and its stakeholders to share knowledge and build relationships. It allows cross-fertilisation of ideas and for each stakeholder to understand the views of others."

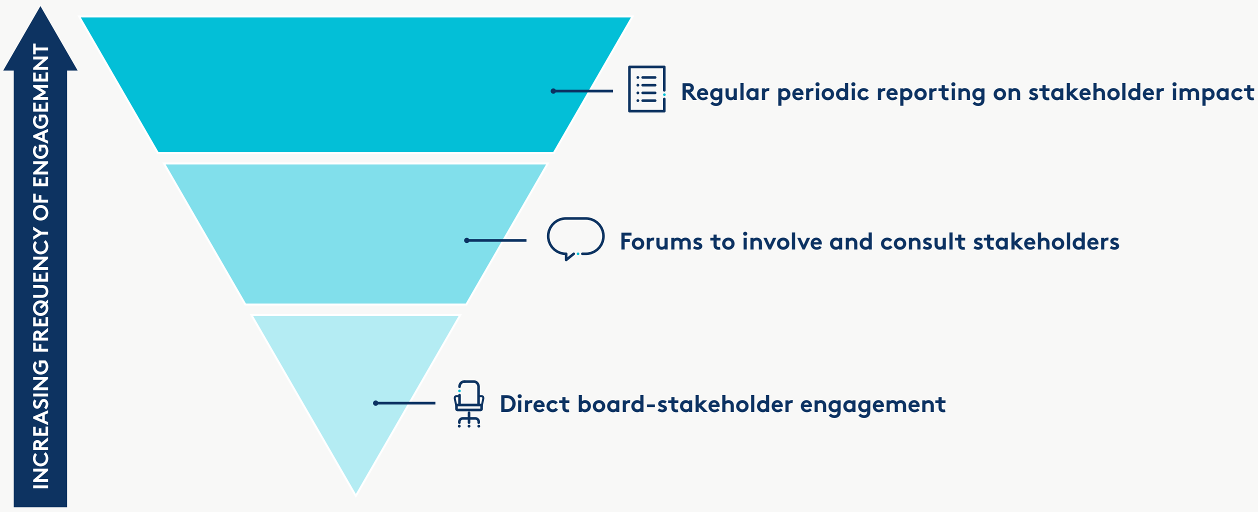
While this is largely management-led, board members participate in the stakeholder days.

Intermediaries such as peak bodies, representative groups or advocacy groups may also be a useful mechanism for stakeholder engagement. These groups have a close ear to the ground and may be aware of serious issues of harm or misconduct long before these issues are widely known, including by management or the board. At the same time, if boards are seeking first-hand perspectives on certain issues, then they must remain alive to the distinction between these groups and rights-holders themselves – a narrower sub-set of stakeholders who may rely on the advocacy efforts of representative groups.

> Organisations may need to think beyond simply engaging with stakeholders on behalf of rights-holders, and instead look to engage with rights-holders directly. Additionally, there will be no goodwill if rights-holders are asked to spend time sharing feedback with the board and then do not see or hear the results.

– Sarah McGrath, Manager, Australian Human Rights Commission.

Fig 2: Type and frequency of engagement



Regular periodic reporting on stakeholder impact

- Board papers that include the 'stakeholder impact', metrics and unfiltered information (e.g. NPS scores, complaints and verbatim customer feedback)
- Surveys of employees or customers, including verbatim comments
- Committee reports that outline stakeholder perspectives
- Case studies presented by management on projects/ issues, outlining differing stakeholder perspectives
- Social media reports (Twitter and Facebook)
- Reviewing Glassdoor

Forums to involve and consult stakeholders

- Advisory Committees and Forums
- Stakeholder days
- Board/stakeholder dinners
- Stakeholder/management presentations
- Site visits and 'town hall' meetings
- Customer advocates

Direct board-stakeholder engagement

- Direct meetings between the board and stakeholders
- Board Committees and designated directors responsible for issues
- Stakeholder reps attending board meetings

Key questions the board should be asking regarding stakeholder engagement:

- Should the board be directly involved in engagement with a particular stakeholder group or on a particular issue?
- Is the board's engagement with each stakeholder commensurate with their importance?
- Has the board considered whether the form of engagement with a particular stakeholder is tailored to that group?

DECISION MAKING

Consider stakeholder voices as part of the board's decision-making processes. Consider disclosing/reporting on decision making and stakeholder impact.

Boards will derive the greatest value from their stakeholder engagement by using that information to not only inform their decision making, but more broadly understand their organisation's operating environment.

This section considers practical steps the chair and board can take when designing board discussion processes to ensure that sufficient consideration is given to stakeholder perspectives.

Meeting agendas, board papers and information

The chair's role typically includes setting the agenda for board meetings (usually in consultation with the CEO and company secretary) and working with management to ensure there is an appropriate flow of information to directors.

Decision making

No matter how information is presented to the board (whether by direct engagement or management presentation/recommendation), it is ultimately up to the board to ask the right questions, consider impacts / risk and make a considered decision. It will not always be possible to reconcile stakeholder interests. However, that should not be the aim – instead, the board should focus on informed, considered decision making with due regard to different perspectives.

The chair, together with their fellow directors, may wish to consider some or all of the following:

- Request that management explicitly address stakeholder perspectives and impact when preparing board papers;
- Allocate time (either as standing items or on an ad hoc basis) at board meetings for presentations from board committees, advisory committees or individual directors (discussed below) tasked with considering certain stakeholder issues;
- Allocate regular time to review information that provides a good temperature check on key stakeholder groups (for example, whistleblowing complaints, customer feedback, employee survey or engagement scores). These mechanisms can also assist a board assess organisational culture;
- At the end of a board item or alternatively at the end of the meeting, the chair may consider asking the board to consider whether there are any issues that have been discussed which require further stakeholder input; and
- Schedule meetings with key stakeholders, either as part of regular board meetings, board strategy days or specific programmes, including site visits or stakeholder days.

Board committees and advisory committees

Boards often delegate to board committees and advisory committees the task of examining certain matters in greater detail. While ultimate responsibility for decision making and understanding stakeholder perspectives sits with the board, it may be appropriate to delegate authority when it comes to particular stakeholder groups or issues. Stakeholder issues are sometimes dealt with in existing risk committees as part of non-financial risk management or in newly formed committees like ethics committees established to consider a wide range of matters. They may also be covered under the broader rubric of sustainability and managed through the relevant committee.

Importantly, subject to their charter, these committees will not usually have the board's decision-making power, although at a practical level they may have more influence in relation to their delegated subject matter.

These committees may be made up of board members only (board committees) or be management led with directors as members or observers (advisory committees). Some advisory committees may also include stakeholder representatives (such as customer and community advisory committees or reference groups). In delegating responsibility to these committees, the board may wish to consider if the committee will undertake direct engagement with stakeholder group(s) and how it will report to the board.

Such board or advisory committees can provide a valuable forum for a deep-dive analysis of key stakeholder issues, concerns and questions ahead of board meetings. They also provide comfort to the board that sufficient time has been allocated to considering important issues.

Advisory committees with stakeholder representatives and directors as observers allow management to take the lead whilst ensuring directors can directly hear the stakeholder voice. These committees can be formalised and meet regularly, or on an ad hoc basis to address specific issues or projects.

If the board, together with management, decides to establish an advisory committee, the organisation must consider:

- the purpose of the engagement;
- the stakeholders it intends to engage with;
- whether it will engage directly with the board or via management; and
- how often the committee should meet.

It will also be important to ensure committee members are well-resourced and provided with a clear remit. In some cases, it may be appropriate to compensate stakeholders for their time commitment given they often have significant resource constraints. It is also important to review the composition of such committees to ensure the committee is not listening to the 'same old voices'.

> Be careful not to overload advisory committees with detailed agendas and responsibilities. These should be discussion forums that enable an opportunity for stakeholders to share key concerns.
>
> –Anonymous director.

We have provided below some case studies of successful committees that operate in Australian organisations. Notably, these structures play an important role in governance for large, listed companies and NFPs alike.

CASE STUDIES:
IAG, ANZ, Flourish Australia

IAG, a general insurer, has a 'Consumer Advisory Board' that is led by the CEO with the CEOs of customer advocacy organisations all participating. The chair always attends (as an observer), and directors are encouraged to attend when they can. This committee provides the board with the opportunity to hear directly from customer advocates about vulnerable and disadvantaged customers who are an incredibly important subset of customers. According to Elizabeth Bryan AM FAICD, Chairman, IAG, "vulnerable customers are not a group that is easy to understand across data. They are a very special group that needs our service. To know what their issues are gives us a lot of insight into what we can do to address their problems." According to Gerard Brody, "for customer advocates like the Consumer Action Law Centre, IAG's Consumer Advisory Board provides a venue where the senior management and board directors can better understand customer vulnerability and the experience of customer's engagement with their business".

ANZ's 'Ethics, Environment, Social and Governance Committee' meets regularly every board period. The committee is comprised of four directors, but according to former Chair, David Gonski AC FAICD*Life*, the whole board usually chooses to attend. The committee's purpose is to "assist the board in providing oversight of measures to advance ANZ's purpose, namely, to shape a world where people and communities thrive, focusing on ethical, environmental, social and governance matters". In practice, it is tasked with thinking about broader issues and impact the organisation might be having, whether the board and management are asking the right questions as well as sharing perspectives from current governance literature and the broader community. Management also decided to replicate the committee at an executive level and also drew considerable value from the process.

Flourish Australia, a specialised community mental health service, engages and partners with the Flourish Australia Community Advisory Council. The Council consists of people accessing Flourish Services, acting as representatives from across metropolitan, regional, rural and remote areas of the states in which Flourish Australia has locations. The intention of the Council is to function "as a link between people accessing various services of Flourish Australia, staff, management, and the Board of Directors". Two examples of this are the way in which the Board benefited from the advice of the Council about service delivery issues and how it could help people stay safe and connected during the COVID-19 pandemic. Post-pandemic, the Board intends to continue to engage regularly with the Council to ensure the services retain the positive changes initiated through its responses to COVID-19. Chair of Flourish Australia, Professor Elizabeth More AM FAICD, explained that "the Community Advisory Council is a valuable guide on important issues with which the Board deals. For instance, the Council has been involved in the development of Flourish Australia's new Strategic Plan and the Monitoring and Evaluation Framework which the Board deeply appreciated."

Reporting and communicating to stakeholders

Consultation raises expectations and it is critical that boards are clear about the outcome. It is therefore appropriate for the board to provide feedback to stakeholders, particularly after interactions where the stakeholder has given their time and resources to engage with the board.

Similarly, as part of its decision-making processes the board should consider which stakeholders will be impacted by and how those decisions should be communicated to the affected stakeholder group. Some stakeholders will prefer that the board directly communicates the decision, while others may prefer to deal with management or require no direct feedback at all.

Boards should also consider whether the organisation is reporting adequately on its stakeholder engagement. In many organisations, the annual report is the main tool for reporting to shareholders and stakeholders alike. Other reports such as sustainability reports or corporate responsibility reports can be important channels for organisations to communicate sustainability performance and impact.

Key questions the board should be asking when considering stakeholder voices as part of decision making:

- How does the board's decision-making process consider stakeholder perspectives?
- Is the board getting the right information about stakeholders (for example, do board papers consider the 'stakeholder impact') and does it allocate sufficient time to consider these issues?
- Does the board have the right structures to enable a deep dive on key stakeholders and/or issues (for example, would an advisory committee support decision-making processes or does the board have a board committee that explicitly encapsulates stakeholder impact in its remit)?
- How should the board report on and/or communicate decisions to impacted stakeholders?

EVALUATION

Evaluate and monitor the ongoing effectiveness of the organisation's stakeholder governance framework and the board's role in stakeholder engagement.

As with all governance processes and relationships, it is important to assess the effectiveness of the organisation's stakeholder governance and adjust as necessary.

Management will likely lead the evaluation of organisational stakeholder governance, but the board should be involved in the review. Similar to other aspects of stakeholder governance, this might not necessarily be a formal process and may simply form part of ongoing risk management processes. It may also involve:

- Directors having informal conversations with stakeholders to get their perspective on the health of the relationship and the effectiveness of the organisation's engagement;
- Cross-checking engagement with other stakeholder groups (for example, speaking to government or advocacy groups to understand how the organisation's approach to stakeholders is being received);

In some circumstances, the board may wish to commission an external party to undertake an independent evaluation which can provide a baseline for future monitoring.

Key questions the board should be asking when monitoring and evaluating the organisation's stakeholder governance framework:

- Does the board regularly review the effectiveness of the organisation's stakeholder governance vision/strategy?
- What independent, external data speaks to the organisation's relations and stakeholder impact?
- Should the board engage an external party to assess the state of stakeholder relations?

Legal duties and current debate

DIRECTORS' LEGAL DUTIES

Under both the common law and *Corporations Act 2001* (Cth) (Corporations Act), directors owe duties to the company to:

- act with care and diligence and for a proper purpose;
- act in good faith in the best interests of the company; and
- not to use their position or information as a director to gain an advantage or cause detriment to the company.

Similar duties are owed by directors of State-based incorporated associations and other non-Corporations Act entities. Responsible persons of registered charities also owe similar duties under the Australian Charities and Not-for-Profit Commission's (ACNC) Governance Standards.[4]

While a director's duty to act with care, diligence and good faith in the best interests of the organisation is currently understood as owing to shareholders as a whole, recent court decisions in Australia demonstrate that directors have considerable discretion under the law when exercising managerial power.

In some sectors, such as human services, health and education, there may be mandated requirements in regulations and/or accreditation frameworks to consult with key stakeholders. Generally, these requirements seek to ensure the voices and experiences of the people who are using the organisation's services are considered in policy making, program design and quality improvement processes.

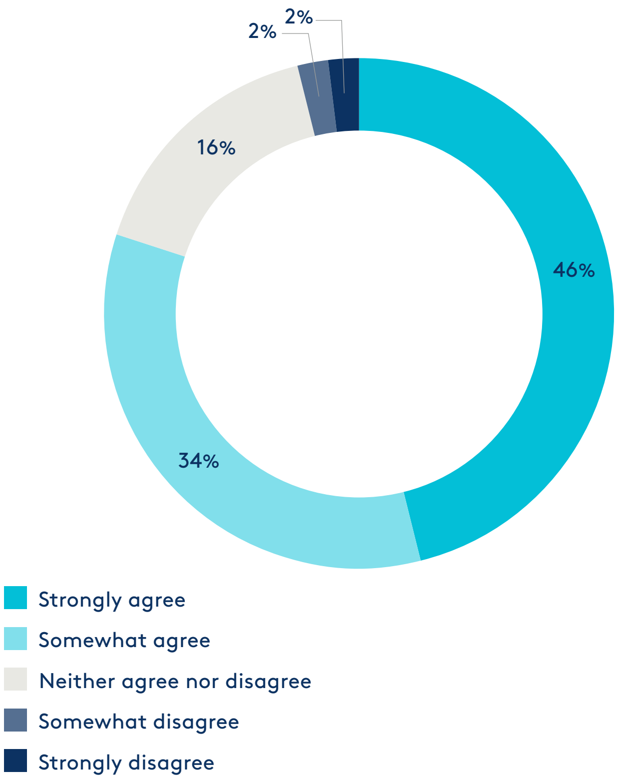
Sometimes, these requirements represent minimum standards for consultation. It is important for boards to think broadly about their overall approach to stakeholder engagement, including any legal obligations they may have to hear from their stakeholders.

It is increasingly recognised that decisions made by a board will have an effect on the organisation's stakeholders including employees, customers, suppliers and the community. The duty to act in the best interests of the organisation cannot be isolated from the interests of other stakeholders. Acting in a responsible and ethical manner towards stakeholders is consistent with, and is often necessary for, promoting the company's interests and sustainability.

4 AustLII. Commonwealth Consolidated Regulations, Australian Charities and Not-for-profits Commission Regulation 2013, Reg 45.25, Governance standard 5 – Duties of a responsible entity, **http://classic.austlii.edu.au/au/legis/cth/consol_reg/acancr2013614/s45.25.html**, (accessed 23 March 2021); Refer also to, AICD, 2019, Not-for-Profit Governance Principles, 2nd edition, Principle 2, January, **https://aicd.companydirectors.com.au/-/media/cd2/resources/director-resources/not-for-profit-resources/nfp-principles/pdf/06911-4-adv-nfp-governance-principles-report-a4-v11.ashx**, (accessed 23 March 2021).

There is evidence too that community sentiment is in favour of legal reform to give greater recognition to stakeholders. A 2021 survey of the general Australian population by Essential Research commissioned by the AICD, showed that 80 per cent of people support there being a legal requirement for companies to consider stakeholder interests beyond shareholders, with only four per cent disagreeing.

Survey snapshot: To what extent do you agree or disagree that large businesses should be legally required to consider the interests of people other than shareholders in their decision making (for example, customers, employees, local communities)?



CURRENT DEBATE: SHAREHOLDER PRIMACY VERSUS STAKEHOLDER CAPITALISM

The longstanding governance debate of shareholder primacy versus stakeholder capitalism has received increased focus in recent years. The staunchest proponents of the shareholder primacy model believe a company's central objective is to maximise returns for shareholders, and that a company has no social responsibility to broader society.[5]

The opposing view advocates the strategic importance of companies considering all stakeholder groups, including shareholders. Under this model, the goals of shareholders and stakeholders are considered compatible and no interest is held to be paramount over another. The principles of the stakeholder capitalism concept do not just permit, but rather require directors to take into account the needs of all their stakeholders (including shareholders, employees, customers, suppliers, communities and the environment) to achieve sustainable growth and create value over the long term.

A more recent perspective on the debate is the reinterpretation of "corporate purpose" – the reason a corporation is created and exists, what it seeks to do, and what it aspires to become – proposed by The British Academy's **The Future of the Corporation** program led by Colin Mayer. Under this model, broad concepts of corporate purpose – "to solve the problems of people and planet profitably, and not profit from causing problems" – are placed at the heart of corporate governance. To achieve this, Mayer suggests the regulatory system should promote an alignment of corporate purpose with social purposes where required and ensure that companies' ownership, governance, measurement and incentive systems are appropriate for this.[6]

5 M Friedman, 1970, "A Friedman doctrine: The Social Responsibility of Business is to Increase Profits", The New York Times, 13 September, **https://www.nytimes.com/1970/09/13/archives/a-friedman-doctrine-the-social-responsibility-of-business-is-to.html**,. (accessed 23 March 2021).

6 C Mayer, 2018, "The Future of the Corporation: Towards Humane Business", Journal of the British Academy, 19 December, **https://www.thebritishacademy.ac.uk/publishing/journal-british-academy/6s1/the-future-of-the-corporation-towards-humane-business/**, (accessed 22 March 2021).

However, speaking in rebuttal to Mayer's proposal at the 2019 Corporate and Commercial Law Conference at the NSW Supreme Court of Australia, Catherine Livingstone AO FAICD, Chair of Commonwealth Bank of Australia, strongly objected to regulating purpose - arguing it undermines the entire concept and would have unintended consequences. Rather than adding to the regulatory challenge, the better approach would be to evolve the regulatory engagement model so corporations and regulators engage in real time to address issues and anticipate problems. Ms Livingstone concluded there was no difference between shareholder primacy and stakeholder capitalism in the real world. But this was not to say that their interests were always aligned.

While stakeholder capitalism was first popularised in the 1980s, its renewed interest has been helped, in part, by increasingly global connected economies, civil societies and environment. COVID-19 has been just one confronting reminder of this global inter-connectedness.

In 2018, BlackRock CEO Larry Fink famously urged every company to articulate its purpose and how it benefits all stakeholders, including shareholders, employees, customers, and the communities in which they operate.[7]

More recently, Larry Fink's '2021 Letter to CEOs' reminds leaders that no time in history has been more important for companies to respond to the needs of their stakeholders. The more companies can show their purpose in delivering value to their customers, employees and communities, the better able they will be to compete and deliver long-term, durable profits for shareholders:[8]

> A company that does not seek to benefit from the full spectrum of human talent is weaker for it - less likely to hire the best talent, less likely to reflect the needs of its customers and the communities where it operates, and less likely to outperform.
>
> – Larry Fink, BlackRock CEO.

Closer to home, the competing approaches of shareholder primacy and stakeholder capitalism were examined in the Australian Financial Services Royal Commission. Commissioner Kenneth Hayne stated "...the best interests of a company cannot be reduced to a binary choice". In his view, a director's duty to act in good faith in the best interests of the corporation demanded consideration of more than the financial returns available to shareholders in any particular period. This correlates with the perspectives AICD members shared as part of the AICD's consultation on its Forward Governance Agenda in 2019. Asked about how AICD members approach the best interests duty in practice, the highest proportion of respondents report that they balance the interest of shareholders and stakeholders (49 per cent) when fulfilling the best interests duty. While 16 per cent consider the interests of shareholders as a whole, and 32 per cent consider stakeholder impacts as relevant to the interests of shareholders as a whole.

According to Commissioner Hayne, while financial returns to shareholders (or 'value' to shareholders) will always be an important consideration, it is not the only matter to be considered.

> The longer the period of reference, the more likely it is that the interests of shareholders, customers, employees and all associated with any corporation will be seen as converging on the corporation's continued long term financial advantage. And long-term financial advantage will more likely follow if the entity conducts its business according to proper standards, treats its employees well and seeks to provide financial results to shareholders that, in the long run, are better than other investments of broadly similar risk.[9]
>
> – Commissioner Kenneth Hayne.

7 L Fink, 2018, Larry Fink's 2018 Letter to CEOs: A Sense of Purpose, **https://www.blackrock.com/corporate/investor-relations/2018-larry-fink-ceo-letter**, (accessed 22 March 2021).

8 L Fink, 2021, Larry Fink's 2021 Letter to CEOs, **https://www.blackrock.com/corporate/investor-relations/larry-fink-ceo-letter**, (accessed 22 March 2021).

9 K Hayne, 2019, Final Report: Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry, Commonwealth of Australia, at p 403, **https://www.royalcommission.gov.au/sites/default/files/2019-02/fsrc-volume-1-final-report.pdf**, (accessed 22 March 2021).

Moreover, increasingly mandated reporting on environmental, social and governance (ESG) issues, such as climate-related financial disclosures and modern slavery reporting, suggest that ESG matters are now part of the board's fiduciary duty landscape, particularly for large or listed companies. Engagement with these topics is often driven by customer, employee, community expectations and in the case of ASX listed companies, ESG-focused institutional shareholders via proxy voting. A company's ability to demonstrate how ESG impacts its strategy, operations, and long-term prospects is therefore important to meeting the needs of all stakeholders.

Further resources

- AICD, 2020, ***General duties of directors***, Director Tool.
- K Schwab, 2021, *Stakeholder Capitalism: A Global Economy that Works for Progress, People and Planet*, Wiley.
- C Mayer, 2017, ***Future of the Corporation***, The British Academy.
- V Hunt, B Simpson, Y Yamada, 2020, ***The case for stakeholder capitalism***, McKinsey & Company.

APPENDIX ONE – STAKEHOLDER PERSPECTIVES:

Adapting the board's engagement to the stakeholder

The AICD asked representatives from diverse stakeholder groups for guidance on the steps that directors should be taking to elevate stakeholder voices to the board.

These representatives shared insights on how boards can engage with the individuals they represent more effectively, the hallmarks of meaningful engagement and examples of where engagement with stakeholders has led to a better outcome for the board, organisation and stakeholders. The following section explores these insights.

CONSUMERS

Effective customer engagement will ensure an organisation gains and retains loyal customers while avoiding consumer actions, boycotts, and reputational damage. Serving customer long-term needs must be at the forefront of all directors' minds.

Limitations of metrics and data

The most common tool boards will use to understand the customer experience is by way of metrics. These may include net promoter scores (NPS), customer feedback/satisfaction and complaint data. Directors must remain alive to the limitations of using such metrics as a 'go-to' reference point for customer satisfaction. The tail of a distribution (particularly regarding complaints data) is often where special vulnerabilities are identified. Significantly, customers' ability to articulate complaints can distort issues (for example, being charged for a service not provided may be categorised as a 'billing issue'). Additionally, the most disadvantaged or vulnerable clients may struggle to make a complaint, and so will be excluded. Boards should be asking: Who are our vulnerable customers? How can our products or services be tailored to their needs?

To get a better picture, directors should be taking steps to understand the worst experience customers have, and systemic issues that may not show up in the data. Asking for more qualitative data from management that examines complaints in detail will help boards contextualise any underlying issues. In the financial services sector, customer committees of the board have been created as a way of enhancing organisational focus on customers with deep dives on specific complaints being one mechanism to grow NEDs understanding.

Direct engagement with customers

There is also value in boards creating opportunities to engage directly with customers. This form of engagement humanises issues and can remind a board and an organisation of its core purpose. This does not need to happen all the time, but there can be a high return on investment when it does. For example, some boards in the healthcare sector start their board meetings with a client story or a client appearing before the board to share their experience with the organisation. This helps keep the board focused on patients/clients and reminds directors of their organisation's impact.

CASE STUDY: Financial Counselling Australia and the Consumer Action Law Centre

Financial Counselling Australia and the Consumer Action Law Centre facilitated a joint project called 'A Day in the Life'. The project invited senior decision-makers, including directors, to spend time with a financial counsellor to better understand the work they do and the issues that people face. By listening to calls on the National Debt Helpline, participants could hear directly from customers experiencing challenges. This project was an incredibly valuable experience that enabled directors to get a first-hand understanding of the financial challenges individuals face.

Gerard Brody of the Consumer Action Law Centre comments that "as a customer advocate, there is very little need to speak to directors directly. However, knowing that directors sit on advisory committees and panels gives advocates comfort that directors are obtaining direct feedback on issues." See **page 24** for a more detailed discussion of advisory committees.

CASE STUDY: The Energy Charter

The Energy Charter, a national collaboration that supports the energy sector towards a customer-centric future, is a unique way that a sector is tackling better stakeholder engagement. As part of its framework, an Independent Accountability Panel produces an annual assessment of achievement of better outcomes for Australian energy consumers. This includes strong examples of customer engagement and areas for improvement. The most recent annual assessment can be found **here**.

The Energy Charter has also produced a Customer Voice @ Board Toolkit that is available **here**.

A number of Energy Charter signatories acknowledged that if they are truly to put customers at the centre of their business, this needs to start from the top, from board and CEO/senior executive level. Initiatives include remuneration and bonuses linked to customer measures; review of customer complaints by management/board; executives listening to customer calls and providing feedback; and senior managers sitting with their contact centre on a regular basis.[10]

10 Independent accountability Panel, 2020, The Energy Charter: Assessment of achievement of better outcomes for Australian energy consumers in 2019-20, December, **https://theenergycharterpanel.com.au/wp-content/uploads/2020/12/IAP-2020-Final-for-publication.pdf**, (accessed 23 March 2021).

The role of customer advocates

In financial services and energy sectors, customer advocates that report directly to the board or management are increasingly common.

According to Alan Kirkland (CEO, CHOICE), there may also be a time and place for engagement by boards with representative groups like CHOICE. It does not need to be regular but can provide invaluable intel. Advocates work at the coalface and are often aware of systemic issues that could have significant reputational repercussions long before senior management.

NFPs – clients or beneficiaries

Often, an NFP's most important stakeholders will be the people that the organisation exists to benefit (its beneficiaries). In some cases, these beneficiaries may be vulnerable people.

We heard that some NFPs elevate the client voice by having client representatives attend all board meetings where they present on specific topics. Often, the board will request that representatives consider a particular topic and call other clients to determine how they feel about the services being provided. This was considered a valuable way for those representatives to feel empowered and heard. Equally, it had a profound impact on the board and decision-making. This form of client engagement requires representatives to be appropriately resourced and well supported.

Refer to the AICD's **Not-for-profit Governance Principles**, Principle 8 for further details about stakeholder engagement in the NFP sector.

EMPLOYEES

Boards generally have greater opportunities for engaging directly with employees than they do for other stakeholder groups, and should look for ways to make the most of this access. In some cases, employees may have longer experiences of working with the organisation than board members, and are often also the closest to the needs and opinions of the organisation's other key stakeholders such as consumers/clients, suppliers and the broader community.

Direct employee-board engagement

While employee surveys, 'town hall' meetings, site visits and floor-walks all provide visibility of workforce issues and dynamics, directors should also establish regular and independent opportunities for engagement with employees that enable their own lens on culture, inclusion, safety and other workplace issues. Ideally, this should be outside of structured forums that risk being manipulated by management. For example, inviting employees to attend board meetings to present and respond to questions on operational issues, projects and initiatives is one effective way for directors to understand the day-to-day workings of the organisation.

> You can do the walk of the shop floor and your 'meet and greets', but we all know there is a level of fake-ness in that. You will never get the level of due diligence you need to have real comfort from this. As a board member, I would want to take much more proactive steps.
>
> – Scott Connolly, Assistant Secretary, Australian Council of Trade Unions (ACTU).

In some cases, boards have invited new recruits to join board meetings and provide their initial impressions of the organisation given they can provide fresh insights before the process of acculturation occurs. Similarly, some organisations have staff liaison committees comprised of employees from different levels and functions across the organisation that report and present to the board or board committees on certain issues.

Equally, directors should remain alive to the possibility that not all employees will feel comfortable with direct contact with the board. It is important that directors pause and reflect on the objective of any employee-board engagement and what forum is most appropriate to facilitate this.

As with other advances in digital technology, social media has empowered employees. In the increasingly virtual environment, employees can be their company's strongest advocates or harshest critics, and what they say may be believed to a greater extent than what any official spokesperson has to say. At the same time, platforms such as Glassdoor are increasingly used by organisations to understand past and present employee perspectives.

Of critical importance is the need for a dedicated channel for boards to hear from employees about serious concerns of misconduct within the organisation. Ensuring the organisation has in place a robust whistleblower policy and reporting mechanism is a fundamental way to enable the board to have an appropriate line of sight.

At the same time, in certain organisations, it may also be appropriate for the board to let employees know that it is open to hearing grievances directly via the chair, particularly where these relate to any improper behaviour on the part of senior management. The chair can then decide whether to raise the concerns with management or bring them to the board for wider investigation on a confidential basis.

In overseas markets such as the UK we are also aware of some organisations having a dedicated in-box for any member of the community to anonymously (or otherwise) raise an issue of concern with the organisation. This can be a useful complement to other formal, internal mechanisms such as anonymous whistleblowing hotlines, in uncovering issues.

Australia's 2021 Edelman Trust Barometer reveals that trust in employers has reached an all-time high, with 78 per cent of Australian's trusting their employer over business and government.[11]

Employee expectations have shifted with worker's health and safety, regular employee communications and upskilling rising as important attributes. Edelman's data also revealed employees are expected to be taken into consideration when making business decisions with two-thirds of employees believing they have the power to force corporations to change and 59% of employees more likely to voice their objections to management or engage in workplace protest compared to previously.

As the world transformed in response to the pandemic, Australians more than ever turned to their employers for guidance, reassurance and information they can trust. The workplace-home divide has been broken down, and employers have embraced a new role in their employee's lives. In an environment that demanded empathy and transparency, a strong bond of trust has resulted between organisations and their people. Having forged this bond, the opportunity exists for business to enrich their culture and drive deeper engagement in the post-COVID era.

– Michelle Hutton, CEO Australia and Vice Chair of Asia Pacific, Edelman.

Workplace advisory committees

Establishing a workplace advisory committee is another effective employee engagement mechanism to provide the board a direct line. Scott Connolly, Assistant Secretary, Australian Council of Trade Unions (ACTU), has seen these structures used well in organisations that are skilled-labour intensive or have legacies of public ownership, for example Qantas. It is important that these structures are "not just set up as listening forums to pay lip-service to", says Scott Connolly. Rather, the key to their success is that they are formalised, resourced and provide a safe forum for open and frank conversations on issues.

The role of trade unions

At the more collective level, senior trade union representatives who were consulted in preparing this guide noted a distinct lack of direct access to boards. Although, it was recognised that escalating matters directly to the board is generally only done when there is dissatisfaction with the way matters are being handled by management. In Scott Connolly's (ACTU) view, "this [lack of engagement] is not only counter-intuitive, but also indicates a failure of governance".

11 Edelman, 2021, 21st Annual Edelman Trust Barometer, **https://www.edelman.com/sites/g/files/aatuss191/files/2021-01/2021-edelman-trust-barometer.pdf**, (accessed 22 March 2021).

Unions and other workplace representatives can provide insights into key risks in a way that may not be possible for management – for example around safety issues, workforce morale and wider cultural challenges. More broadly, unions indicate that organisations should seek to build better relations with them, moving beyond transactional interactions, such as during workplace bargaining negotiations.

Director feedback is that industrial relations matters tend to be reported to the board for visibility and stress-testing, but that senior management would generally retain responsibility for engagement and dispute resolution. Directors do, however, acknowledge there is scope for a greater role to be played by the board where, for example, employee relations issues pose a significant threat to the organisation's risk profile and there is a need to support management to find a circuit-breaker.

Trade union representatives expressed optimism that boards will begin to take more proactive steps to engage with workforce issues. This will only be enhanced as the role of superannuation funds and other progressive voices in capital markets begin to spotlight workforce issues to affect change. In Daniel Walton's (AWU) view, "it will give a greater line of sight for employees about what's happening in an organisation (wage theft is just one example)".

Climate change illustrates the power of capital to affect change. People are looking at disclosure and reporting. In 20 years, workforce issues will be where climate is now. There is a clear risk to organisations and we are actively pointing this out to investors both directly and through their shareholders.

– Scott Connolly, Assistant Secretary, Australian Council of Trade Unions (ACTU).

SUPPLIERS

Respectful up-chain relationships with creditors and suppliers can significantly impact an organisation's profitability and the way it operates. Zero-sum game approaches to engaging with suppliers (if the supplier wins, the company loses), and squeezing the lowest price, is now widely considered myopic business practice. Instead, by establishing a mutually valuable relationship with key suppliers, an organisation can achieve longer-term cost savings, in the form of reduced issues with availability, quality and delays in supply. Notably, this requires a shift in mindset from cost-based, transactional or even an adversarial way of thinking to a more value-based, collaborative way of thinking.

From a small business supplier perspective, a core and consistent challenge is navigating the obvious power imbalances when dealing with big business. This is particularly acute regarding supplier/creditor concerns around unfair contract terms and payment times – both often issues that boards can have little to no visibility of unless they know what they are looking for.

Although supply chain and creditor relations are principally an operational function, the board has a clear role in setting expectations of management for maintaining healthy supplier and creditor relations. This extends to expectations around the types of reporting boards would like to see on legal compliance – particularly contract terms and payment times, as well as fairness in dispute resolution. An organisation may also wish to survey suppliers to see how they regard the organisation.

Specifically, Former Australian Small Business and Family Enterprise Ombudsman, Kate Carnell, challenges directors to be curious on how the company's standard form contracts measure up against unfair contract terms law, as well as how quickly suppliers are paid.

Most boards would agree that supplier/creditor invoices should be paid in 30 days or less. Similar to work, health and safety issues, standard payments times and how long it is taking to pay a supplier/creditor is something that needs to be reported to the board, and at a pretty granular level.

– Kate Carnell, Former Australian Small Business and Family Enterprise Ombudsman.

To help address supplier concerns, the *Payment Times Reporting Act 2020* (Cth) (which commenced on 1 January 2021) introduces a new requirement for large organisations and certain government enterprises to report on their payment terms and practices in relation to small business suppliers. Notably, the new legislation requires that all reports be provided to the board, while granting the regulator a naming and shaming power for non-compliance.

FIRST PEOPLES

Boards have a responsibility to ensure that stakeholder voices that are not ordinarily heard have such an opportunity. Aboriginal and Torres Strait Islander communities undeniably fall into this category. The destruction of ancient Aboriginal rock shelters at Juukan Gorge by Rio Tinto is just one tragic example of the First Peoples stakeholder voice being lost or ignored in a corporate decision-making process.

Organisations need a principled approach to engagement with First Peoples, and the board must ensure this forms part of a stakeholder governance vision. Organisations must engage early and invest in the relationship. A 'tick-a-box' approach to engagement led by or managed by a corporate affairs team with limited board/management oversight is not satisfactory. It can be perceived as disrespectful, empty and meaningless.

Taking time to understand traditional owners' or Aboriginal and Torres Strait Islander protocols and timelines for consultation is also critical for effective engagement. Cultural awareness training is one way that directors can prepare for engagement with Aboriginal and Torres Strait Islander communities, while sending an organisational signal that respectful relationships with First Peoples are important. As with other stakeholder groups, engagement should be ongoing and genuine, not just when a specific approval/consent is needed. There should be a foundational and ongoing connection that demonstrates a strong relationship and recognises historical legacies.

Developing a Reconciliation Action Plan (RAP) program is another way that organisations can support the national reconciliation movement and engage with First Peoples. Boards can send a clear signal about the importance of reconciliation through their active oversight of RAP implementation.

Interviews have identified that traditional owners value direct board-to-board engagement. This should occur 'on Country' and does not necessarily need to be frequent. Engagement should not be overly formalised and 'minders' (corporate affairs or legal representatives) should be left behind. For traditional owners, such engagement shows respect and recognition and humanises the relationship. It is an opportunity for boards to get out of "the bubble" and see First Peoples in their own community.

Traditional owners and First Peoples have long memories. According to an anonymous stakeholder representative, "boards must acknowledge that there is still a lot of trauma in the room and be accepting of and ready for the rawness of the feedback".

Further resources: International best practice in Indigenous engagement

Indigenous advocates recommend that organisations have regard to the United Nations (UN) Declaration on the Rights of Indigenous Peoples, which Australia has supported since April 2009. It calls on States to obtain free, prior and informed consent of Indigenous people before adopting legislative or administrative measures that would affect them. Although mandated at the State and legislative level, the declaration provides an international articulation of best practice expected in engaging with Indigenous people which is also instructive for corporates and other organisations. Key elements of the declaration include:

- Free should imply no coercion, intimidation, or manipulation.
- Prior should imply that consent has been sought sufficiently in advance of any authorisation or commencement of activities and that respect is shown for time requirements of Indigenous consultation/consensus processes.
- Informed should imply that information is provided that covers a number of matters, including: the nature, size, pace and scope of any proposed project or activity; the reason(s) for or purpose(s) of the project and/or activity; areas that will be affected; preliminary assessment of the likely economic, social, cultural and environmental impact.
- Consent to any agreement should be interpreted as Indigenous peoples have reasonably understood it. Consultation and participation are crucial components of a consent process.

The declaration can be found **here**.

ESG ISSUES

Human rights issues

For organisations, human rights cannot be simply framed as a reputational or 'non-financial' risk. The consequences of poor human rights practices can materially impact a company's stakeholder relationships, financial performance and prospects for sustainable value creation.[12] Focus on human rights as an issue has increased significantly over recent years. Since the Declaration of Human Rights, Australia has become the signatory to a number of conventions, treaties and convents to enshrine the rights of people from particular population groups and backgrounds. These include the Convention on the Rights of the Child, the Convention on the Rights of Persons with Disabilities and the Declaration on the Rights of Indigenous Peoples. Goals and obligations set within these declarations and conventions also flow into legislative and policy frameworks at the Commonwealth and State and Territory levels and place responsibilities on organisations for effective outreach and engagement to minority groups and stakeholders.

What constitutes human rights?

Human rights is clearly defined in several international conventions to include traditional issues such as child labour, forced labour, human trafficking, modern slavery, freedom of association, and indigenous people's rights.[13] The concept has expanded to include access to proper nutrition, water and sanitation services and emerging issues such as freedom of expression and privacy on the internet and sustainable fair wages. All issues that can impact an organisation's ability to do business.

Australia's *Modern Slavery Act 2018* (Cth) entered into force on 1 January 2019 and requires organisations of a certain size to provide a statement on modern slavery risks in their operations and supply chains, and to take steps to address these risks. This was a decisive step by the Commonwealth Government that has elevated modern slavery issues (and arguably human rights issues more broadly) to the boardroom.

Further resources: Modern slavery

Refer to the following AICD modern slavery tools for guidance:

Modern slavery risk oversight – a practical tool to assist directors with their oversight role of modern slavery risk in their operations and supply chains.

What directors need to know about signing off on modern slavery statements – a tool prepared with law firm Herbert Smith Freehills to provide directors with clear guidance on what they need to know about signing off on modern slavery statements.

In considering human rights issues, the board should ensure that the organisation has taken steps to understand if human rights risks exist in the organisation or its supply chain.[14] As part of the board's responsibility for overseeing culture, it should also ensure robust systems are in place to manage and identify any human rights risks and that management has the resources and commitment to do this work.

The board should also probe management on how they have undertaken due diligence and ensure that consultations with communities or 'rights holders' consider language, cultural and other potential barriers to effective engagement. Co-design principles of engagement should also be considered to step beyond mere consultation on projects. Timing is also critical – due diligence should take place before supply arrangements are agreed or before ground is broken on a project, for example.

12 G S Dallas, 2015, "Human Rights Through A Corporate Governance Lens", Harvard Law School Forum on Corporate Governance, 22 May, **https://corpgov.law.harvard.edu/2015/05/22/human-rights-through-a-corporate-governance-lens/**, (accessed 22 March 2021).

13 United Nations, 1948, Universal Declaration of Human Rights (UDHR), **https://www.un.org/en/about-us/universal-declaration-of-human-rights**, (accessed 22 March 2021); International Labour Organization, ILO Conventions, **https://www.ilo.org/dyn/normlex/en/f?p=NORMLEXPUB:12000:0::NO:::**, (accessed 22 March 2021); United Nations Human Rights Office of the High Commissioner, 1976, International Covenant on Civil and Political Rights (ICCPR), **https://www.ohchr.org/en/professionalinterest/pages/ccpr.aspx**, and International Covenant on Economic, Social, and Cultural Rights (ICESCR), **https://www.ohchr.org/EN/ProfessionalInterest/Pages/CESCR.aspx**, (accessed 22 March 2021).

14 G S Dallas, 2015, "Human Rights Through A Corporate Governance Lens", Harvard Law School Forum on Corporate Governance, 22 May, **https://corpgov.law.harvard.edu/2015/05/22/human-rights-through-a-corporate-governance-lens/**, (accessed 22 March 2021).

CASE STUDY: TIMBY

TIMBY, a collaboration between activists, journalists, technologists and designers, is a tool which impacted communities can use to document impacts and provide a feedback loop to organisations (and in some cases boards) on an organisation's impact on a community. Members of an impacted community can take photos, tell stories, and filter this back to organisations directly.

Boards operating in remote communities may wish to consider using TIMBY to understand their organisation's impact.

Amy Sinclair GAICD of the Business & Human Rights Resource Centre is of the view that "boards should consider appointing non-executive directors with specific human rights knowledge and experience. This would bring a whole new perspective by enabling a human rights lens to be applied to issues." Another mechanism that directors have to create accountability is to develop KPIs linked to remuneration that are focused on human rights outcomes.

Further resources: UN Guiding Principles on Human Rights

In 2011, the UN Human Rights Council endorsed these **Guiding Principles** to help states and corporations navigate their respective duties and responsibilities regarding human rights. These principles provide recommendations for a corporation to follow, including how to assess and anticipate relevant human rights issues that may affect the corporate process.

Guiding Principle 16 states that organisations "should express their commitment to meet [their responsibilities for respecting human rights] through a statement of policy that is approved at the most senior level of the business enterprise". This makes it clear that corporate responsibility for human rights must be integrated at the highest levels of corporate governance, suggesting the important role the board must play.

The principles also emphasise the importance of human rights due diligence and how this differs from traditional notions of due diligence. The prevention of adverse impacts on people is the primary purpose of human rights due diligence. It concerns risks to people, not risks to business which traditional notions of business due diligence entail.

Environmental issues

As risks from environmental issues, such as climate change and water scarcity, become increasingly acute, particularly with growing investor activism, boards must understand how these issues impact the organisation's strategy and performance.

Boards should consider whether the collective has appropriate skills and experience, mindful that a baseline level of understanding will be required by all directors. It may be helpful to ask questions such as:

- How capable is our board to effectively oversee climate risk management at our organisation? Do we need to undertake further education?
- Should we recruit senior management and/or directors with experience and exposure to material climate change issues that the organisation faces?
- Do we need to engage with external experts to get an unfiltered perspective on climate risks?
- How will our organisation engage with stakeholders (including local communities) to understand key environmental risks?

Boards should also ensure that management is well-resourced to address environmental issues and whether existing processes are adequate to identify risks. Boards also need to be able to test management to see that they have consulted the relevant internal and external stakeholders to ascertain environmental risks. Given the nature of environmental issues, boards need to be asking questions about the near and long-term risks, mindful that management may have personal incentives to prioritise short-term outcomes.

Notably, it was observed that in some organisations there is insufficient communication between the board and management on environmental concerns that have been raised. This generally involves assumptions being made within the organisation that engagement with stakeholders is being taken care of.

Environmental issues must have sufficient agenda time at board meetings and consideration should be given to whether a 'Sustainability Committee' of the board is necessary to explore issues in greater depth.

Further resources: World Economic Forum and Climate Governance Initiative Principles

The World Economic Forum and the Climate Governance Initiative (CGI) have developed the following principles - **How to Set Up Effective Climate Governance on Corporate Boards: Guiding principles and questions.** These principles, together with resources produced by CGI, aim to educate and equip non-executive directors to build their understanding of climate change so that they may play a proactive role in stewarding their companies' climate transition strategies.

Refer also to Chapter Zero: The Directors' Climate Forum **resources**.

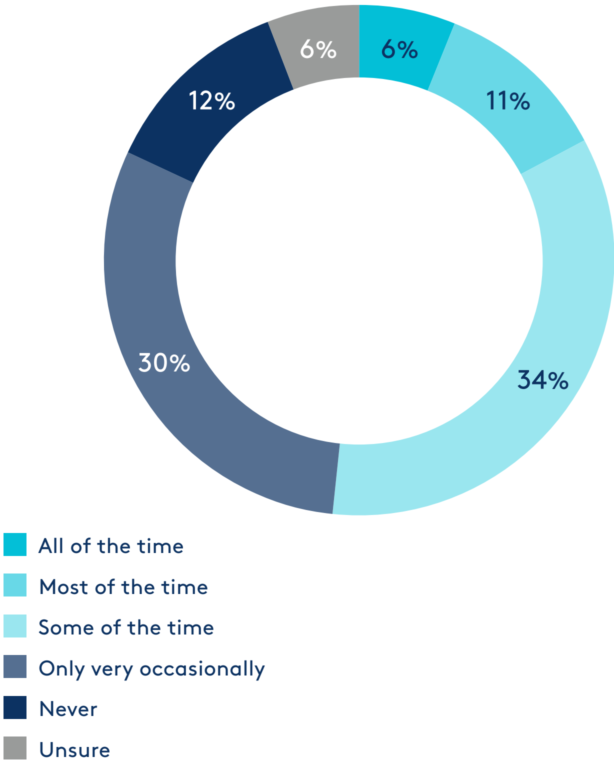
COMMUNITY

The definition of a 'community' stakeholder group is broadening. When it comes to engagement with the community, for many organisations today, this can encompass a number of people who affect (and are affected by) their business activities, ranging from local charities, community groups and residents to local business, councils and elected government officials. It will be important to consider who is purportedly represented by interest groups and whether they are a true reflection of broader sentiment. Indeed, in some cases, influential individuals who may be completely unaffected by an organisation's activities may begin a campaign (often leveraging social media platforms) against an organisation.

Engagement with this vast group of stakeholders can not only benefit the community, it can also improve an organisation's decision making, reputation and competitiveness – by tapping into local knowledge, reducing conflict and building trust. Indeed, a 2018 survey of AICD members in collaboration with KPMG revealed that directors considered the local or regional community in which their organisation operated as the third most critical stakeholder for Australian boards (35 per cent), while the general public was ranked as the fifth most important (16 per cent).[15]

However, a recent survey of the general Australian population indicates that the broader community currently has a sceptical view of the extent to which organisations consider the interests of their stakeholders other than shareholders in their decision making. A 2021 Essential Research survey commissioned by the AICD, showed that just seven per cent of people think that companies consider the interests of the wider community all the time. Rather, 34 per cent of people think that companies consider stakeholders other than shareholders some of the time, while 30 per cent think this is only very occasionally.

Survey snapshot: How frequently do you think Australian large businesses consider the interests of people other than their shareholders in their decision-making (for example, customers, employees, local communities)?



The results also illustrate there is a disconnect between community expectations and corporate priorities. 38 per cent consider that increasing returns to shareholders is the top priority of large Australian organisations.[16]

Critically, however, only seven per cent considered that increasing returns to shareholders should be the top priority for Australian organisations – ranking as the lowest ranking priority amongst those surveyed. Respondents indicated that providing quality products or services, staff safety and wellbeing, as well as complying with laws and regulations should be top priorities for organisations.

15 AICD and KPMG, 2018, Maintaining the social licence to operate: 2018 KPMG-AICD Trust Survey, **https://assets.kpmg/content/dam/kpmg/au/pdf/2018/state-of-trust-survey-2018.pdf**, (accessed 22 March 2021).

16 Essential Research Survey, 1,092 respondents (27th January 2021-1 February 2021).

Survey snapshot: In what order of priority do you think large business owners and directors currently consider the following factors when making decisions?

Broader community expect top three priorities for Australian organisations currently to be:

38% Increase returns to shareholders or investors.

18% Complying with the laws that regulate the organisation.

18% Providing quality products or service.

Survey snapshot: In what order of priority do you think large business owners and directors should consider the following factors when making decisions?

Broader community expect top three priorities for Australian organisations should be:

28% Providing quality products or services.

24% Staff safety and wellbeing.

23% Complying with the laws that regulate the organisation.

Just **7%** of survey respondents consider that increasing returns to shareholders should be a top priority for Australian organisations.

These perspectives broadly correlate with a 2019 nationwide survey of the general public and business leaders on expectation of business and business priorities, undertaken by the Committee for Economic Development of Australia (CEDA).[17] General public respondents ranked providing staff with a good work/life balance for employees, providing highest quality products and investing in staff wellbeing as what should be business' top priorities. While for business leaders, providing products/services that are better tailored to customer needs, increasing shareholder returns and providing staff with training and/or career development ranked the highest. Notably, these results demonstrate that organisations' leadership clearly see business as having a breadth of responsibilities that extend beyond financial performance - challenging the simplistic notion of a clash between shareholder and broader stakeholder interests.

17 CEDA, 2019, 2019 Company Pulse Survey, **https://cedakenticomedia.blob.core.windows.net/cedamediacontainer/kentico/media/general/publication/pdfs/companypulsefinalspreads18sep.pdf**, (accessed 22 March 2021).

APPENDIX TWO –

Interview methodology and acknowledgements

The AICD conducted in-depth individual interviews with stakeholder representatives and leading directors operating in various sectors. Interviews lasted 30 – 60 minutes. The discussion was framed by open-ended questions to explore the experience and perspectives of the interviewees. The semi-structured interview process was used flexibly in each of the interviews where prompts were used to elicit deeper information in some of the interviews while in others, participants drove the discussion themselves.

We wish to acknowledge the following stakeholder representatives, directors and contributors for their insights and reflections.

STAKEHOLDER REPRESENTATIVES

- **Gerard Brody,** Chief Executive Officer, Consumer Action Law Centre.
- **Kate Carnell,** Former Australian Small Business and Family Enterprise Ombudsman.
- **Melinda Cilento,** Chief Executive, CEDA; Co-Chair, Reconciliation Australia; Non-Executive Director, Australian Unity.
- **Scott Connolly GAICD,** Assistant Secretary, Australian Council of Trade Unions (ACTU).
- **Castaly Haddon,** Stakeholder and Policy Manager, Council of Small Business Organisations Australia (COSBOA).
- **Sabiene Heindl,** Executive Director, The Energy Charter.
- **Alan Kirkland,** Chief Executive Officer, CHOICE.
- **Sarah McGrath,** Manager, Australian Human Rights Commission.
- **June Oscar AO,** Aboriginal and Torres Strait Islander Social Justice Commissioner, Australian Human Rights Commission.
- **Alix Pearce,** Campaigns Director, The Climate Council.
- **James Pearson,** Chief Executive Officer, Australian Chamber of Commerce and Industry.
- **Gerard Reilly,** GM Communications, Powerlink Queensland; Chair of Industry Working Group, The Energy Charter.
- **David Ritter,** Chief Executive Officer, Greenpeace.
- **Amy Sinclair GAICD,** Regional Representative for Australia, New Zealand and the Pacific, Business & Human Rights Resource Centre.
- **Dr Katrena Stephenson GAICD,** Director, Environment, Development and Community, Kingborough Council.
- **Daniel Walton,** National Secretary, Australian Workers Union.
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- **Professor Elizabeth More AM FAICD,** Chair, Flourish Australia.
- **Fiona Payne GAICD,** Chair, Therapy Focus, 360 Health + Community and Victory Life Centre; Community Member, Brightwater Care Committee; External Member, South Metropolitan Health Service Board People, Culture & Engagement Committee; Elected Member, AICD WA Division Council.
- **Gabrielle Trainor AO FAICD,** Director, Infrastructure Australia, Zurich Australia Limited, WAM Global, ACT City Renewal Authority, Major Transport Infrastructure Authority (Vic), Western Parkland City Authority, Charlie Perkins Education Trust; Chair, Construction Industry Culture Taskforce, National Film and Sound Archive; Commissioner, Australian Football League (AFL).

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About us

The Australian Institute of Company Directors is committed to strengthening society through world-class governance.

We aim to be the independent and trusted voice of governance, building the capability of a community of leaders for the benefit of society. Our membership of more than 45,000 includes directors and senior leaders from business, government and the not-for-profit (NFP) sectors.

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