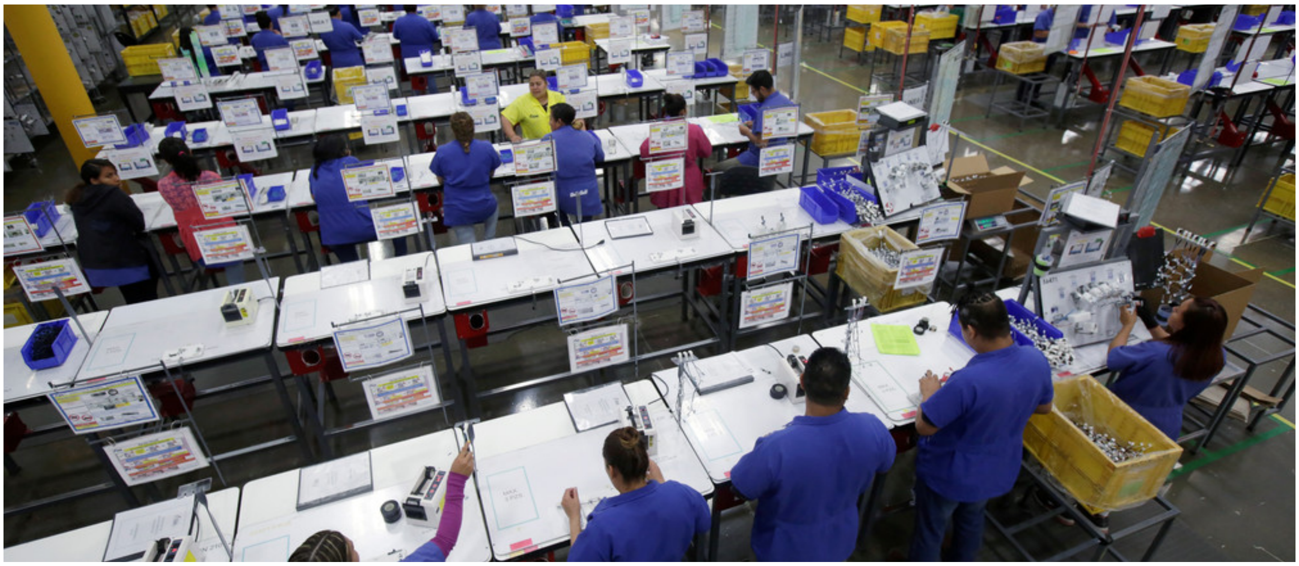
WORLD ECONOMIC FORUM

Questions directors need to ask in the age of stakeholder capitalism



A company's stakeholders include employees, suppliers, customers and communities. Image: REUTERS/Jose Luis Gonzalez

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- Shareholder capitalism is making way for stakeholder capitalism.
- Not taking this approach can, for some companies, seriously threaten their licence to operate.
- Companies need to look at how robust and fit for purpose their stakeholder governance is.

The past year has seen significant developments that indicate a systemic shift towards purposeful business and responsible capitalism, challenging well-e
their corporation will play in society and what steps they must take to ensure their corporation is prepared for the future.

In corporate governance terms we are now entering the age of stakeholder capitalism, as we anticipated in a White Paper published last year. 2019 may y
focus by boards on stakeholder governance and on long-term sustainable stewardship by the investor community.

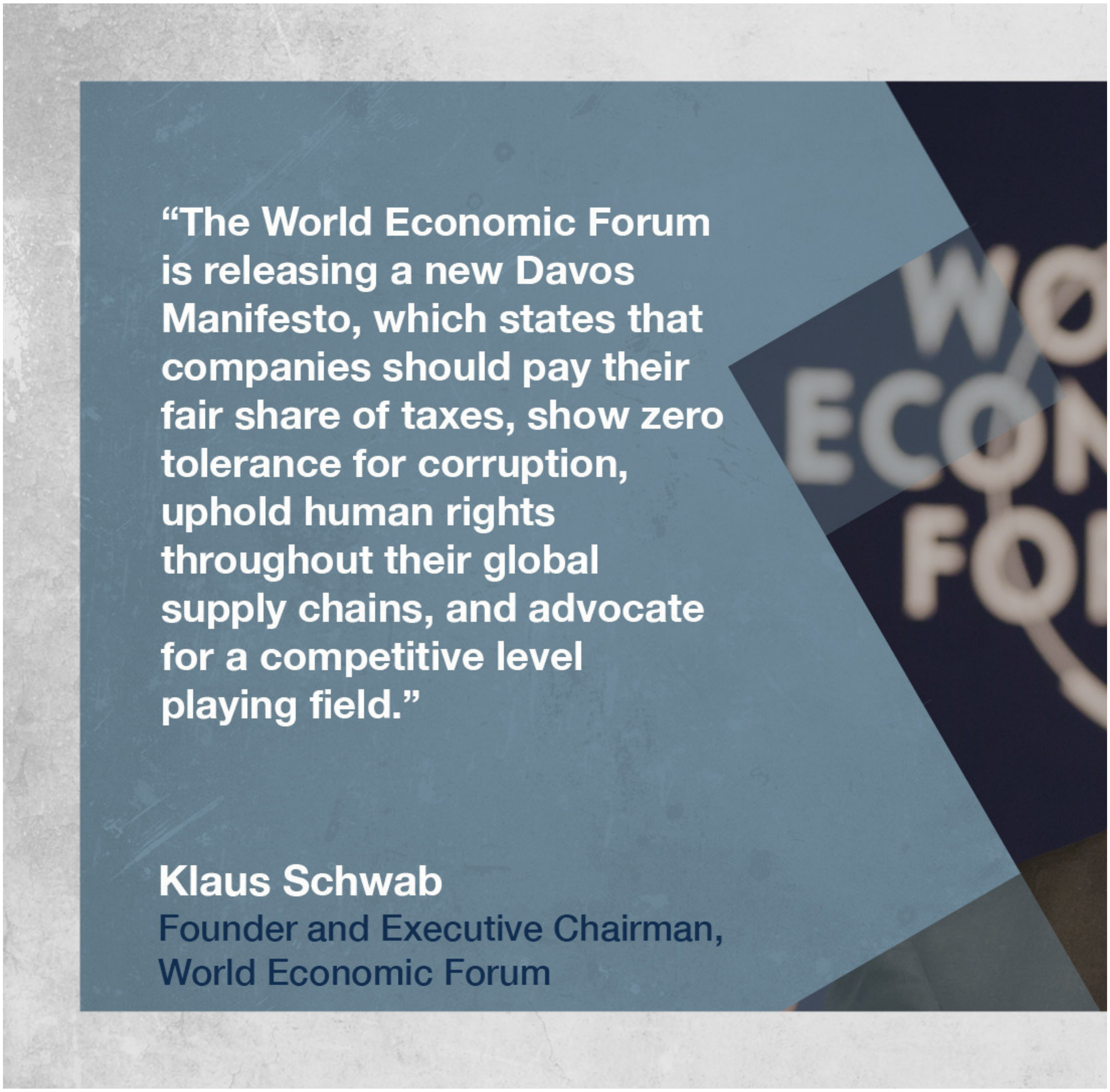
There have been some important steps that support a new age of stakeholder capitalism.

1) August 2019 – The Business Roundtable Statement on Corporate Purpose signed by 181 North American CEOs essentially embraced stakeholder capi
for the benefit of all its constituents and not solely to maximize shareholder wealth;

2) December 2019 – The British Academy's publication of their Principles for Purposeful Business which posited that corporate law should place purpose

3) November 2019 – The Institute of Directors published a Manifesto for Corporate Governance in which they advocate 10 specific policy proposals desig
stakeholders and wider society; to improve the competence and professionalism of UK board members – whose role is central to business decision-makir
addressing the challenge of climate change.

4) December 2019 – The World Economic Forum launched a new Davos Manifesto: The Universal Purpose of a Company in the Fourth Industrial Revoluti
50th anniversary.



Contrary to what many boards and commentators understand, shareholder primacy is grounded not in law, but in the teachings of business schools influe

Stakeholder capitalism has, in fact, been grounded in Anglo-Saxon corporate law for some while, especially in the two jurisdictions with the highest conce
corporate laws of civil jurisdictions, the most advanced example being in The Netherlands, where it has been imbedded in corporate law for some years n

In UK law, through the enlightened shareholder approach in the Companies Act 2006, which requires directors to promote the success of the company fo
employees, suppliers, customers, communities and the environment), the likely consequences of any decisions on the long term, the desirability of the co
members of the company. Recent UK corporate governance reforms now require many UK companies to report on how boards have complied with this d

The late Professor Lynn Stout best articulated the position under Delaware law in her 2012 paper: "Shareholder primacy had become dogma, a belief syst
where they had first learned of it."

She explains very succinctly: "Put bluntly, the principal-agent model is wrong. The first incorrect factual claim is that shareholders "own" corporations. As
themselves, holding property in their own names, entering their own contracts, and committing their own torts.

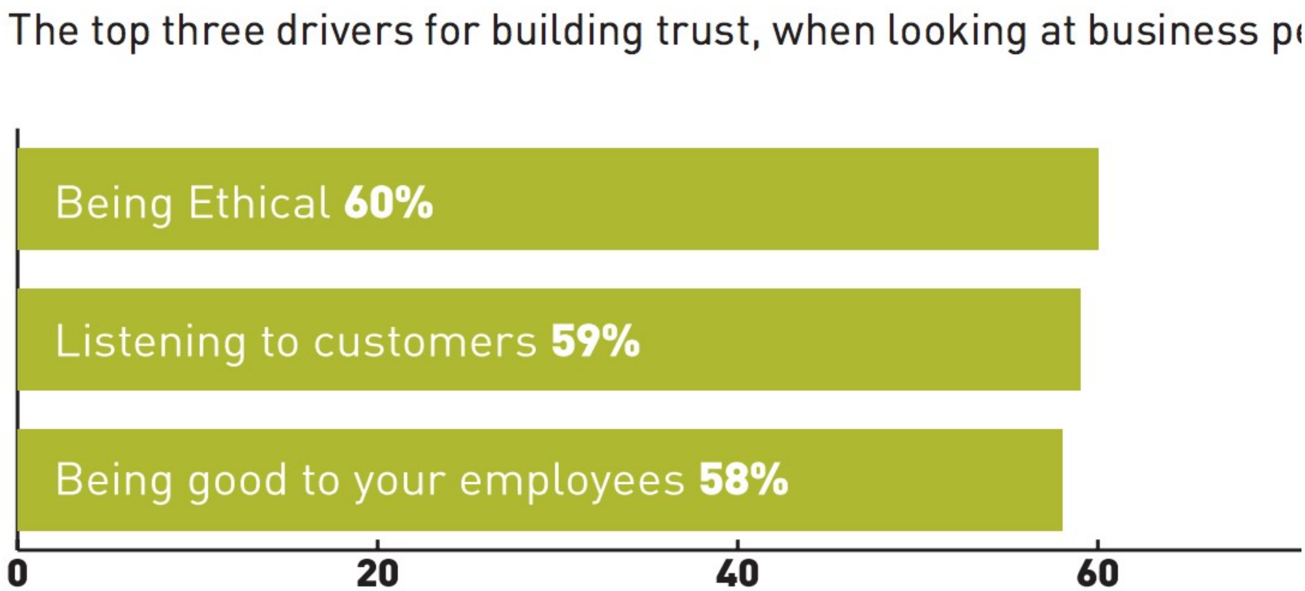
What do shareholders own? The label "shareholder" gives the answer. Shareholders own shares of stock, and shares in turn are contracts between the sh
Ford doesn't entitle you to help yourself to the car in the Ford showroom). In a legal sense, stockholders are no different from bondholders, suppliers, and

Directors need to be aware of their legal responsibilities as members of the board. Good corporate governance is all about understanding roles, responsib

In the words of Lord Cadbury in his report of 1992: "Governance is the system of rules, procedures and processes by which a company is directed and cc
professionally managed." At the heart of directors' responsibilities and what should be their guiding star is the fact that directors are trustees of the compa

As mentioned before, there is one area where the laws or approaches of various countries are beginning to converge and that is in the area of stakeholder
stakeholders.

Stakeholders can mean any parties interested in or affected by the operations of the company and, in addition to shareholders, are generally divided into e



Businesses that win the trust of their stakeholders will prosper over the long term.

Not taking this approach can, for some companies, seriously threaten their licence to operate. Acting in a way that promotes the success of the company
consider present and future shareholders, so there is a need to balance short and long-term interests.

It is largely up to directors to determine how success can be achieved, and indeed how to define success (subject, of course, to shareholders' specific ins
success for shareholders will include addressing environmental, social and governance (ESG) matters and integrating them into the company's strategy ar

Against this backdrop, CEOs and Boards are faced with a myriad of challenges arising from macroeconomic, geopolitical, societal and tech externalities. T
corporations and its leadership; and the dilemma of how best to balance short-term and long-term decision-making, especially in light of the focus by mar

Data is the new currency to chase for the creation of new opportunities, but is also making it difficult for companies to influence the conclusions made abc
cost, are no longer accepted business behaviour, especially by newer generations. At the same time, the focus on traditional financial reporting metrics is
capitalism.

So what more can boards do? In addition to pursuing generally accepted good governance practices, companies need to look at how robust and fit for pu
pursue these all the way through the company and its subsidiaries, wherever they might be located.

They should ask questions such as:

• have we a clear understanding what our fiduciary duties are and who we owe them to?

• do we really understand who our key stakeholders are, internally and externally?

- have we tested our strategy with regards to the impact it has on our stakeholders? have we integrated them across our strategy?
- how effective is our engagement with them? should we engage directly with key stakeholders, rather than relying on management alone to do so?
- are we bringing our stakeholders' voices into the boardroom? How well do we, as a board, communicate with and listen to our stakeholders?
- are our purpose and our values strong enough for the whole company to embrace the highest standards of business integrity, thereby helping us attract
- do we have the appropriate skills to understand the risks and opportunities presented to our business by the environment, especially climate change?
- how well do we communicate to our shareholders/investors our progress as regards the above? what reporting standards do we follow?
- do we have the right leaders, in terms of personal qualities and experience, which this generation can trust?

As my colleagues Beatriz Araujo, Julia Hayhoe and I continue our work on the Future Face of the Corporation with the World Economic Forum, we invite w

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The views expressed in this article are those of the author alone and not the World Economic Forum.

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