Going Beyond Corporate Governance: Sustainability Reporting

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Good corporate governance involves a commitment of a company to run its businesses in a legal, ethical and transparent manner - a dedication that must come from the very top and permeate throughout the organisation. That being so, much of what constitutes good corporate governance has to be voluntary. Law and regulations can, at best, define the basic framework - boundary conditions that cannot be crossed. I am always of the view that while law may need to be strengthened when occasions so demand, there are fundamental limits to using legislative and regulatory instruments to enforce better compliance from the Corporates to partner the Government in achieving National or Social objectives. Therefore, the thrust of the day should be voluntary adoption of good practices and development of 'Corporate Citizenship' by the industry as a whole.

An active, well-informed and independent Board is necessary to ensure highest standards of corporate governance. Auditors should also be independent and rotation of the auditors has become a sine-quo-non in the light of the recent corporate frauds world over.

Regulatory agencies are trying their best not only in the legal, effective and credible enforcement but also in safeguarding the interests of the investors and the economy as a whole from any kind of disturbance. We feel that Institutional investors can also play a significant role by effectively contributing to strengthen the working of entities towards the righteousness.

While progress is being made in getting discussions of issues such as Corporate Governance, Corporate social responsibility, climate change and ethical sourcing on to the agenda, others argue that it is also important to distribute responsibility for these issues across the board rather than relying on one or two individuals and as companies start to see corporate responsibility not only as a case of simply introducing community investment programmes but also as part of how they operate their supply chains or manage their energy efficiency. As larger groups of executives are participating in senior-level discussions, there is evidence that sustainability issues are being incorporated into strategy, research and development, as well as business activities of the companies throughout the Globe.

Companies pool capital from a large investor base both in domestic and in the international capital markets. In this context, Investment is ultimately an act of faith in the ability of a company's management and the ability of a company's management is fully dependent if there are the good practices which are being followed by it. Therefore, the need is to strengthen the corporate governance so that the following may be achieved.

- To promote or to increase awareness among entrepreneurs adoption of good corporate governance practices, which are the integral element for doing and managing business.
- To ensure the quality of audit that is at the root of effective corporate governance by making the Auditor accountable for the disclosure of financial information.
- To make the Board of Directors as well as the CEOs and CFOs accountable for the discharge of their duties with the proper use of their rights within the powers.
- To form an appropriate system in order to check the Directors independence in the board and to monitor the work of Audit firms.

- To pay special attention in the quality and effectiveness of the legal, administrative and regulatory framework.
- To increase the shareholder activism i.e. the exercise and enforcement of rights by minority shareholders with the objective of enhancing shareholder value over the long term.
- To infuse India’s Business Culture with a “Spirit of Corporate Governance” in order to maintain sustainable and effective corporate governance.
- To implement more robust Bankruptcy Laws which are a key component of any corporate governance system?
- To eliminate “Regulatory Arbitrage” i.e. to establish a clear mandate for each regulatory Authority for the enforcement of Clause 49 of the Listing Agreement, thereby improving India’s corporate governance enforcement mechanism.
- To resolve the conflict between the dominant shareholders and the minority shareholders by improving the rights of minority shareholders.

Corporate governance is a system of making Management accountable towards the stakeholders for effective management of the companies. Corporate governance is also concerned with the morals, ethics, values, parameters, conduct and behaviour of the company and its management. The underlying principles of corporate governance revolve around three basic inter-related segments. These are:

- Integrity and Fairness
- Transparency and Disclosures
- Accountability and Responsibility

Ministry of Corporate Affairs (MCA)had set up a National Foundation for Corporate Governance (NFCG) in association with the Confederation if Indian Industries (CII), Institute of Chartered Accountants Of India (ICAI) and other National level organisations as a not-for-profit trust to provide a platform to deliberate on issues relating to good corporate governance, to sensitize corporate leaders on the importance of good corporate governance practices as well as to facilitate exchange of experiences and ideas amongst corporate leaders, policy makers, regulators, law enforcing agencies and non- government organizations. The foundation has been set up with the mission to:

- Foster a culture for promoting good governance, voluntary compliance and facilitate effective participation of different stakeholders;
- Create a framework of best practices, structure, processes and ethics; and
- Make significant difference to Indian corporate sector by raising the standard of corporate governance in India towards achieving stability and growth.

To highlight the frauds and irregularities in the corporate sector the issues of governance, accountability and transparency in the affairs of the company, as well as about the rights of shareholders and role of Board of Directors have never been as prominent as it is today. With the integration of Indian economy with global markets, industrialists and corporations in the country are being increasingly asked to adopt better and transparent corporate practices.

The degree to which corporations observe basic principles of good corporate governance is an increasingly important factor for taking key investment decisions. If companies are to reap the full benefits of the global capital market, capture efficiency gains, benefit by economies of scale and attract long term capital, adoption of corporate governance standards must be credible, consistent, coherent and inspiring. Hence, in the years to come, corporate governance will become more relevant and a more acceptable practice worldwide in a holistic manner.

However, the financial and operational performances are no longer the exclusive drivers for business. Business community is no longer expected to merely make profits. How that profit is made is also important to investors and stakeholders. Increasing public consciousness and stricter government regulation have resulted in growing demand for disclosure. And hence Economic, Social, and Environmental factor are now being recognized to play an important role in business success. This recognition along with the encouragement from internal and external stakeholders has led the companies to perform in these areas, which has resulted in surfacing of sustainability reporting. There is paradigm shift in measuring and reporting sustainability performance. With burgeoning globalization India is bracing itself to keep up with the international competition.

In India, the history of non financial reporting can be dated back to 1993 with the notification from the Ministry of Environment and Forests, Government of India to submit environmental audit reports by any industry, operation or process requiring consent to operate within the Water (Prevention & Control of Pollution) Act, 1974, the Air (Prevention & Control of Pollution) Act, 1981 or both or authorization under the Hazardous Wastes (Management and Handling) Rules, 1989 published under the Environment (Protection) Act, 1986. The term 'Audit' was replaced by 'Statement' being self submission by industry vide another notification by the Ministry of Environment and Forests, Government of India.

As per the IFC Sustainable Investments Country Report 2009, numerous organisations, such as TERI, the Confederation of Indian Industry (CII) and IFC itself, are active in promoting corporate responsibility and sustainability reporting. Environment Social Governance (ESG) disclosure by Indian companies in the form of corporate sustainability reports and responses are slowly improving, but from a very low starting point. Another baseline study conducted by the Emerging Markets Disclosure Project (EMDP) in the end of 2009 on corporate environmental, social and governance (ESG) reporting trends among the largest publicly traded companies in emerging markets suggests that the level of sustainability reporting in India is still evolving.

However, gradually more of the Indian companies are recognizing the challenge of going global and are using the voluntary reporting approach as a market-based instrument during the last five to six years ago. For almost all of these companies, the GRI Guidelines is the reference point against which reports are being prepared.

The Movement of Non-Financial Disclosure in India

In the year 2000 GRI promoted the sustainability reporting guidelines in the South Asian region for the first time. Large companies like the **Tata group of companies** started reporting for the last ten years and now followed by many from the conglomerate, construction, computers, mining, chemical, health products, energy, oil & gas, energy, banking, automotive, food and beverage sector of Indian industry. Although there are 56 companies disclosing information to environment and social performances, a total of approximately 40 companies refer to the GRI Guidelines, although with varying application levels and assurance approaches. While currently there are no officially recognized guidelines or reporting standards on sustainability reporting (by accounting or regulatory bodies), the Indian companies are becoming increasingly oriented towards the globally accepted guidelines, the GRI framework. Over 80% of these reports correspond to application level a (or A+), the remainder was either undeclared or lower level of adaptation. The breath of the reports and their coverage of most GRI Indicators prove that Indian reporters are committed but the number of such commitments needs to grow at a much faster rate than what it is today compared to other emerging economies like Brazil, South Africa and China.

From the list of sustainability reports registered in the GRI website, it is observed that many companies like ITC, Reliance Industries, Jubilant Organosys, Dr Reddy's, are the leading companies with almost 6-7 years of experience on sustainability reporting, however there are many companies from other sectors like engineering and construction e.g., L&T, Mahindra & Mahindra of the auto sector; Infosys and Wipro Technologies from ICT sector; SIDBI and ABN Amro from the banking sector which have come up with innovative approaches of report presentation and establishing reporting process only in the recent past. It is noteworthy that the five industrial sectors with the highest market value are petrochemicals; manufacturing; infrastructure; telecommunications; and banking which are showing interest in developing their sustainability reports in the near future.

GRI has established its training programmes though four certified training partners from various constituencies like industry association, mediating agency and civil society to impart training to Indian companies. However the demand for training has increased many folds which are not being met adequately. Professional institutions like ICAI and ICWAI could take a leading role to proliferate such knowledge and skills on the topic amongst Indian companies.

In December 2007, a move had been set in motion by the central regulating - Reserve Bank of India (RBI) which would expect major banks to play a pivotal role in sustainability issues by sensitizing their clients on the issues related to human rights and environment and develops sustainability reports.

In 2008, CRISIL announced the launch of the S&P ESG India Index, the first index of companies whose business strategies and performance demonstrate commitment to meeting environmental, social and governance [ESG] standards and incorporate sustainability measures into their investment decisions. Fifty Indian companies that meet certain ESG criteria were drawn from the largest 500 companies listed on the National Stock Exchange of India. However, the disclosures on environmental and social performance by companies were quite low amongst the 50 companies who participated in the index.

In 2010, the Department of Public Enterprise has constituted a working group consisting of leading public sector enterprises to improve on the CSR Guidelines. The DPE is also including the aspect of sustainability reporting as per GRI Guidelines into these voluntary guidelines.

Global Movement of Non-Financial Reporting and Government's Role

Globally, we have seen enormous growth in sustainability reporting, with nearly 3,000 reports published in 2007. These reports increasingly come from emerging markets. While in 1998, Asia, Africa and Latin America only published a few reports, by 2007, countries like Brazil, China, India and South Africa published almost 10% of all reports globally. In Brazil, sustainability reporting has risen exponentially, having tripled in the last five years. China seems set to replicate this reporting boom, but at an even faster rate. The South Africa's JSE stock exchange is requiring listed companies to integrate their sustainability reports with their annual reports, with effect from July 2010. According to a report in *Business Day* newspaper Prof. Mervyn King, chairman of the King committee and a leading expert on governance, said: “South Africa is among the first countries in the world to require integrated reporting of listed companies. This puts us ahead of the game.”

In June 2010, the recently completed GRI global conference, GRI proposed that all large and medium-sized companies should publicly report on their – material – environmental, social, and governance performance issues by 2015 or explain why, if they don’t. On the other hand, many governments across the world are setting examples on sustainability reporting. Some examples are:

1. In 2002 Sweden was the first country to require sustainability reports from state-owned companies. Guidelines for external reporting by state-owned companies got published in November 2007.
2. In December 2008, the Netherlands government released its Statement on International Corporate Social Responsibility in the Netherlands

3. The Danish action plan for CSR got released in May 2008 and hundreds of the largest private and state-owned companies and institutional investors in Denmark included corporate social responsibility information in their annual financial reports beginning in 2010.
4. In China, the government has been the key driver behind encouraging the uptake of corporate social responsibility (CSR) by Chinese companies. Indeed, it is still the case that most of the companies reporting in China are state-owned enterprises.

With the above background, considering these developments world over, the following measures/ initiatives are under way in India.

Initiatives by Ministry of Corporate Affair

Throughout India, stakeholders including, customers, communities, investors, regulators and non-governmental organizations are asking questions to corporate about how they are managing across “triple-bottom-line”. The need to communicate effectively with various stakeholders has taken precedence in many Indian companies.

To facilitate the companies on this Ministry of Corporate Affairs came out with voluntary guidelines on corporate social responsibility (CSR), in 2009. These guidelines incorporate all Ten Principles of the United Nations Global Compact. The Ministry of Corporate Affairs believe that corporate India has a major role in nation’s socio-economic development. These CSR guidelines are India’s realization that various developmental challenges should be addressed in conjunction with sustainable corporate growth.

The Ministry also has a mechanism for voluntary disclosure for companies. Those companies willing to disclose information on sustainability simply can do so by filling up a form, designed by the Ministry. An easy mechanism like this motivates more and more companies to come forward on transparency.

Ministry of Corporate Affairs has also issued National Voluntary Guidelines for the Social, Environmental and Economic Responsibilities of business in 2011. One of the principles of National Voluntary Guidelines recognizes the challenges of social and economic development faced by India and builds upon the development agenda that has been articulated in the government policies and priorities.

Other Initiatives

Confederation of Indian Industries (CII) took another initiative with a 'Mission on Sustainable Growth' towards realising the objective of ecologically sustainable economic and industrial growth. The role of CII is to handhold companies in pursuing ecological sustainability and assists industry units to reduce and conserve resources by carrying out energy, water and waste utilization studies to help them in implementation and monitoring. The focus of this mission is on 'high impact' sectors such as thermal, transport, building and construction, cement, etc. So far around 400 companies have signed the mission. The activities taken up under the mission include; ecological footprint for the whole country, and disseminate and provide relevant information on sustainability.

Standardization of reporting is another important aspect of disclosure. The process of collecting and publishing information about sustainability performance is of limited value if companies fail to use standardized disclosure approach. It is important for the companies to speak the same language to facilitate comparisons of performance over time and against competition.

With every passing year, the disclosure for companies reporting on social and environment factors is increasing. The CII ITC Centre of Excellence for Sustainable Development (CESD) is one of the GRI certified training partners in India.

Another initiative is carbon disclosure project. This is a joint effort of CII, WWF-India and a team of Carbon Disclosure Project (CDP), to encourage more and more companies to voluntarily disclose their greenhouse gas (GHG) emissions. With every passing year the disclosure of Indian companies to the CDP has been improving in terms of content and comprehensiveness of the understanding climate impacts on business. For CDP 2009, a total of 44 companies from as many as 13 sectors responded. It is encouraging to see that many Indian corporations already measuring, reporting and managing their GHG emissions.

Then there is Indian Green Building Council rating – LEED India. LEED-India provides building owners, architects, consultants, developers, facility managers and project managers the tools they need to design, construct and operate green buildings. The rating system provides a roadmap for measuring and documenting success for every building type and phase of a building lifecycle. Such a rating system compels the corporations to disclose relevant information.

To facilitate the investors in broadening their investment criteria to include environmental, social, and corporate governance (ESG) conduct of the firms, whose stock they want to invest in, there is an ESG index. It's an initiative of CRISIL, Standard & Poor's and KLD Analytics and Research. The index relates companies ESG performance to stock market performance. The question is how such an index adds to disclosure. The index provides a platform where certain factors serving as proxies suggest good governance of stakeholder relations. These factors include company ESG disclosure, and its public commitment to corporate responsibility and corporate governance.

Finally, I'll like to conclude by highlighting India's progress towards reporting, which remains indisputable. In a short span of time much has been achieved. Ministry along with non-governmental bodies are working towards spreading the understanding and implementation of disclosure and reporting across various sectors.

It is true that small and medium enterprises are not fully aware nor fully appreciate the benefits of sustainability and its disclosure. But we are working towards first making them understand the concept of sustainability and later moving to transparency.

The best-run companies, large and small, are responding to demands and challenges of greater accountability and transparency proactively. While others, having realised the magnitude of impacts of these challenges are taking corrective measure reactively, thereby progressing towards a trend of undertaking proactive initiatives for long-term sustainability that is integrated in the business of companies.

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