Corporate governance: reporting corruption risks and human rights

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The results of this year's edition of the 'ESG analysis of companies in Poland' project were not a breakthrough in the corporate governance area. Over a half of the analysed companies received lower scores in this area which is a result of a rather selective approach to fulfilling disclosure obligations and a lack of consistency in the completeness of reported information over years. All in all, the companies manage their corporate governance issues pretty well when compared to the environmental or social area. This is the outcome of quite strong regulations, legislative requirements imposed and enforced by the legislator as well as market expectations. However, there are two topics that should be underlined as they will be challenging for companies in the light of the changes in the company's reporting and management. These topics are linked to a new understanding of corporate governance that is combined with compliance and ethics which refer to fighting corruption and bribery as well as the necessity to manage human rights.

Legislative challenges

2016 and 2017 are the years that bring changes to the corporate governance area and approach to reporting.

The Accounting Act has been amended to comply with the provisions of the Directive 2014/95/EU of the European Parliament and the Council of 22 October 2014 on non-financial information disclosure.At the beginning of the year, the amended Good Practices of Companies Listed on the WSE entered into force. Additionally, since 3 July 2016, new requirements of the Market Abuse Regulation (MAR) have been applied, which has significantly influenced the existing reporting rules for listed companies. The above changes alone might be challenging for managers. Companies have to conduct a thorough analysis of the surrounding environment and its own operations to report the required information in a correct way. The responsibility for identifying which information is material, price-forming and valuable for the stakeholders and regulator is shifted on companies. This is a great challenge if we consider how the Polish entities have been engaged in non-financial data reporting and sustainable development so far. The challenge can be illustrated with statistics prepared by the Global Reporting Initiative (GRI). GRI is a leading promoter of the non-financial data reporting idea that actively supports organisations in this respect by providing them with ready-to-use solutions for sustainable development. The GRI database currently gathers almost 35,000 social responsibility reports, of which over 24,000 have been prepared in line with the GRI reporting guidelines. The reports have been submitted by about 9,500 organisations from all over the world. It is enough to mention that currently there are only 184 reports registered by companies from Poland.

Market challenges

Recently, we have observed more and more changes on labour and consumer markets as well as in investor's expectations.

Consumers are more active in their search for products and services that are in line with the sustainable development philosophy. These actions are not limited to their own purchasing decisions that are made in line with their own beliefs. Social media enable consumers to share information with hundreds or even thousands of other people just within a few seconds and websites often feature pictures of rotten food, low-quality products or descriptions of unethical business practices by different service providers. Consumers take action and express their protest on the streets. The negotiations related to the planned signing of trade agreements between Europe and Canada as well as the US (respectively CETA and TTIP) mobilised hundreds of people to take to the streets to fight, as it was expressed during the protests in Hanover in April 2016, for fair global trade. Additionally, students of the Cambridge University protested against their university's investments in companies from the oil and gas sector.

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Finally, the companies themselves boost their actions in the non-financial area and raise the bar for their competitors, distinguishing themselves by taking more creative and unexpected CSR initiatives. One example is offering an additional day off to employees whose children go to school for the first time or preparing social responsibility reports that cover a wide range of issues, such as the impact of the latest legislative changes on the whole financial sector.

Business challenges – corruption and bribery

Apart from legislative challenges, companies still face challenges linked to business and management. A good example is the issue of corruption and bribery which falls within the new information disclosure regulations.

Fighting corruption and bribery is one of integral elements of corporate governance and the compliance system. The company's management team should aim at determining framework for countering corruption and bribery in a form of independent documents or through implementing a cohesive system of interconnected regulations and actions. At first glance, one may doubt whether corruption is still an important issue in Poland. After all, according to the report prepared by Transparency International every year, Poland ranks 30th among the least corrupt countries (169 countries are assessed). The situation is constantly improving, Poland's ranking in 2015 was a bit better than in 2014 (climbed one position). There are, for sure, many countries whose level of corruption in the public sector is significantly higher than ours. However, it is worth noticing that still many companies think the issue of corruption is common in their everyday operations. According to the 14th Global Fraud Survey 'Corporate misconduct – individual consequences' carried out by EY, 34% of Polish respondents think that corruption practices are widely spread in the Polish business. Additionally, 26% of respondents are of an opinion that offering gifts, entertainment or money can be justified if it aims at helping the company to survive in the economic crisis. Thus, it seems that creating an effective anti-corruption policy and its implementation will still be a challenge for management teams for some time. In practice, anti-corruption measures should not be bare internal instructions, but rather an active support and promotion of ethical behaviour and transparency in the company's actions and its internal structure. The company's demonstration of responsibility and its consistent approach will surely translate into increased stakeholders' confidence.

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Business challenges – human rights

Another challenge for companies may be linked to ethical business practices, namely compliance with human rights. The most important aspect that we consider here is the issue of forced and child labour. This year, another edition of the Walk Free Foundation study has been published, presenting a number of modern slaves basing on geographical distribution. The modern definition of the notion 'slave' is a bit different than the one defined in history books. In the 21st century, forced labour is not only about human trafficking but also unfair wages, excessive work, employee harassment, mobbing, physical or psychological violence to prevent employees from resigning from work. Modern slaves do not trust public administration bodies which, in their opinion, are often ineffective and powerless. According to the Walk Free Foundation study, as many as two thirds of modern slavery prevails in Asian countries, which is not surprising for many people. However, what can be surprising is the estimation that in Poland there are about as many as 180,000 slaves. This is the worst score in the whole European Union and it places our country on the 24th position in the ranking that shows an estimated proportion of slaves against the total population.

Ethical standards

There is no doubt that international ethical standards are one of the useful tools that companies may employ to create policies and prepare reports on the issues of corruption and bribery as well as human rights. However, the standards should not be considered as an inconvenient requirement that is very often imposed by international clients but rather as an opportunity for development, a starting point to implement a compliance management system and create one complete management system for dealing with ethical requirements.

Ethical audits are carried out in hundreds of Polish companies every year. They are usually commissioned by international corporations which in this way verify the quality of management of ethical issues in their supply chains. The aspects that are verified include product quality, efficiency of logistics and, primarily, responsibility for working conditions, wages and occupational health and safety. A reference point for these kinds of ethical audits are international and widely accepted standards and ethical tools, such as SA8000, EcoVadis, SMETA, BSCI.

Renowned international guidelines are without a doubt a good and comparable benchmark that provides information about the quality of internal procedures at suppliers. They comprehensively handle ethical management by covering a wide spectrum of issues – from human rights, forced and child labour, through occupational health and safety, HR policy, to management systems. Their implementation is voluntary but applying for an external certification according to one or a few standards brings a number of benefits. First of all, it increases competitiveness towards suppliers and exporters. It is not only an asset but even a pass to establishing cooperation with big players on the market that more often include compliance with ethical standards among their supplier requirements. One certified ethical standard may substitute a number of separate ethical audits carried out at the company by its clients.

The certification positively affects the reputation and brand image, improves the company's relations with stakeholders and its closest surroundings. It also increases the company's value on the labour market, both in the eyes of existing and potential employees who can more easily identify themselves with the company's strategy and operations if they see a cohesive approach towards ethical matters in practice. We should also mention the chance companies get to effectively prepare themselves for crisis situations as they learn how to manage them more efficiently thanks to the above-mentioned tools. Finally, there are also more obvious benefits, such as compliance with changing law, including accounting regulations that are being amended or public procurement rules that gradually cover more and more aspects linked to ethical business practices.

Ethical standards – support in reporting

Ethical standards are a good starting point to conduct an analysis of operations and identify key non-financial areas, namely, the areas that companies should report to their stakeholders. It should be underlined that the essence of reporting is not about reporting each and every aspect but reporting only this information that is material to us and our stakeholders. Thus, in order to properly identify the material aspects, the company should carry out a thorough analysis of particular areas of its operations and its relations with the surrounding environment to look for risks of negative impact on people and environment.

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The media regularly report about a factory being shut down because it polluted local groundwater, accidents at drilling platforms or a sharp decrease in share value due to forced or child labour incidents in supply chains. Actions that may seem insignificant and that often are less important than everyday operations that can be measured in financial results may result in severe consequences for the company and its shareholders.

One question appears: how to conduct an efficient analysis? The first step should be to identify market trends, the direction in which the non-financial data reporting is heading. What is the market benchmark? What actions are taken by our competitors and the market? Is this a good reference point? Special attention should also be paid to the company's regulatory environment. The definition of 'regulatory environment' covers not only provisions of law but also norms and good practices outlined by international organisations and authorities, good practices for listed companies, specific industry standards. The market analysis will perhaps show that we cannot really increase our sales without implementing ethical standards that are required by out potential clients. Perhaps our sector lags way behind other sectors and our company has a chance to become the sector leader in terms of sustainable development and positively distinguish itself by creating strategies and social initiatives. And what about our stakeholders? What are their expectations? Firstly, it is really beneficial to determine, during an external analysis, what parties affect our organisation and what parties are affected by us. Secondly, it is also useful to communicate with our stakeholders and such communication should be conducted in a form adjusted to the category of people with whom we want to communicate (e.g. clients, investors, local communities). We can organise workshops or dialogue sessions, distribute materials or conduct direct and individual talks with stakeholders. All methods are good as long as they lead to effective communication, exchange of ideas and expectations. The external analysis is the first step to outline non-financial areas that are material to our company.

The next step is to conduct an internal analysis. Its priority is to understand the way in which the company functions, its internal specificity, strategy and long-term targets. The best source to gain this knowledge is to conduct talks with internal stakeholders of the company, namely, employees who are responsible for specific non-financial areas, including the environment, HR, procurement and supply chain management, health and safety, compliance and internal communication, that are material.

It is crucial to understand processes that take place within the company from the regulatory perspective as well. To look at the implemented documents as well as the organisational and capital structure of the company through the prism of the already identified relations with the surrounding environment. In this way we are able to identify gaps in our current operations that should be taken care of, in terms of potential risks, weakened elements that are not efficiently controlled.

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Non-financial indicators, for example those covered by the GRI standard, are a kind of a general set of rules that should be applied globally by all companies in all sectors, regardless the company's size or character. This should be borne in mind while defining a catalogue of indicators that we decide to use in our reporting. Our final choice may be affected by a number of factors that might make it impossible to create a limited set of indicators. That is why it is so crucial to conduct a thorough analysis of the company and consider all aspects of its operations. Does the company have an extensive supply chain? Does is use a large group of sub-suppliers and subcontractors located in high-risk countries? Does is operate in an industry that is particularly exposed to contact with public entities and take part in many public tenders? Is the safety of employees at risk due to the specificity of work? Has the company implemented material ethical tools, such as a code of ethics or whistle-blowing channels to report non-compliance? These and other questions need to be answered before we make the next step – reporting theses issues to our stakeholders.

Summary

The legislative changes introduced this year, increasing regulatory pressure as well as global political and social attitudes are new challenges for companies. This means that they have an increased responsibility for actions they take and information they publish. It is not possible to completely eliminate the risk of non-compliance but if the company stands on a strong ethical foundation that is supported by comprehensive corporate governance, it can quite effectively manage this risk. Not all situations can be anticipated but it is possible to be prepared for at least some scenarios in order to more effectively manage crisis situations when they appear. Corporate governance and ethical standards it covers are the key tools which make facing new challenges a bit easier. But what is important, in accordance to this year's analysis results, they should be used in a consequent and credible way.

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