



Creating Metrics for Corporate Governance and Sustainable Development

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Standard & Poor's





Creating Metrics for Corporate Governance and Sustainable Development

- **Overview of corporate governance debate and role of corporate governance scoring**
- **Defining governance: financial stakeholders versus broader stakeholder based**
- **Assessing comparative corporate governance structures in an international context: is there a global standard?**
- **Moving beyond the financial approach to governance to sustainability metrics**





Corporate Governance: Recent Research

- Investors cite governance practices as important as financial performance in evaluating investment opportunities
- Investors are willing to pay a premium for shares of a well-governed company
- There is mounting evidence linking corporate governance and financial performance

No internationally recognized standards or benchmarks



What Standard & Poor's is doing

Standard & Poor's has established a capability to objectively benchmark and compare a company's corporate governance practices including:

- **Corporate Governance Scores**
 - *Interactive analytical process*
 - *Done with consent of company: self selecting*
 - *Coverage will take time to build*

Process of measuring corporate governance provides greater transparency for investors and a positive incentive for companies to improve their governance standards:

- **Market based solution**
- **Complements top down efforts by regulators and exchanges**
- **Tool for investors, companies and regulators**

Standard & Poor's Corporate Governance Services

Basic Principles: What is corporate governance and how to measure it?

- At its most basic level – the interaction of a company's management, board directors and shareholders to ensure that all financial stakeholders (shareholders and creditors) receive their fair share of the company's earnings and assets
- A corporate governance score (CGS) is Standard & Poor's opinion on the extent to which a company adopts codes and guidelines of generally accepted corporate governance practices that clearly serve the interests of its financial stakeholders
- Non-financial stakeholders (eg employees, community, environment, etc) not explicitly covered with current methodology. Scope for future extension.



Corporate Governance Analytical Framework

Company Analytical Structure

- ❑ Ownership Structure and External Stakeholders
- ❑ Investor Rights and Relations
- ❑ Transparency & Disclosure
- ❑ Board Structure & Process

Country Analytical Structure

- ❑ Market Infrastructure
- ❑ Legal Infrastructure
- ❑ Regulatory Environment
- ❑ Informational Infrastructure

Standard & Poor's Corporate Governance Services: Company Scoring Criteria

Ownership Structure & External Stakeholders

- *Transparency of Ownership*
- *Concentration and influence of ownership*
- *Influence of external stakeholders*

Investor Rights and Relations

- *Voting and shareholder meeting procedures*
- *Ownership rights*
- *Stakeholder Relations*

Transparency & Disclosure

- *Quality and content of public disclosure*
- *Timing of, and access to, public disclosure*
- *The audit process*

Board Structure & Process

- *Board structure and independence*
- *Role and effectiveness of the board*
- *Board/executive compensation*

Governance Scoring Criteria:

Is there a global standard?

- **Governance structures and philosophies differ globally**
 - *Shareholder versus broader stakeholder focus*
 - *Legal and cultural dimensions*
 - *Examples*
 - One tier versus two tier boards
 - Concentrated ownership versus widely held ownership

- **Principles-based approach**
 - *Fairness*
 - *Transparency*
 - *Accountability*
 - *Responsibility*

Need to interpret individual structures through lens of overarching principles that should be relevant in a global context



Moving beyond the financial approach to governance to sustainability metrics

Business Model

- **What is the value proposition: who would use this and why?**
- **Mainstream versus “specialist” investors**
- **Focus on corporate social responsibility: ethical perspective**
- **Focus on sustainability as a risk factor: financial perspective**
 - *Intangible Asset*
 - *Contingent Liability*



Moving beyond the financial approach to governance to sustainability metrics

Analytical Issues

- **Objective measures for qualitative criteria**
- **Data quality to support measurement of qualitative criteria**
 - *Need for more robust disclosure and reporting*
- **Many individual measurements (multidimensional scaling) or one composite measure**
- **If a composite measure, how to weight diverse variables**
- **Empirical linkage of sustainability benchmarks and company performance**

Moving beyond the financial approach to governance to sustainability metrics

Analytical Framework: New Metrics

- ***Natural Capital***
 - Use of energy and renewable resources
 - Pollution
 - Recyclability

- ***Human Capital***
 - Training and development
 - Diversity and equal opportunity
 - Workplace safety and relations

- ***Social Capital***
 - Community engagement
 - Corporate philanthropy
 - Costs/benefits to local economy