

Corporate Accountabilities

Responsible Governance Practices

A corporation with responsible governance practices fosters a culture of accountability, implements high standards of ethics, focuses on long-term sustainability and aligns the interests of management with the interests of its shareholders. One of the most essential functions of governance is the oversight of management, and holding it accountable for achieving the long-term success of the corporation. A responsibly governed company takes into consideration that its long-term sustainability is also aligned with the best interests of its *stakeholders* (e.g., employees, customers, community and the environment). Decisions that compromise concerns of a corporation's shareholders and stakeholders may result in short-term financial gain, but can also increase risks to the organization, damage its reputation and cause financial losses over the long term. As a result, a company with responsible governance practices is attendant to the interests of shareholders and stakeholders, and is more likely to be a socially responsible company.

Engagement on governance-related issues with companies supports the Critical Concerns and Direction Statement of the Sisters of Mercy because good governance practices are critical to ensuring that a company is responsible on the environmental and social concerns they articulate, such as a commitment to inclusiveness, fair treatment of persons and environmental sustainability. Shareholders engage companies on a variety of governance issues; the following is an overview of current themes in governance engagement. This list will vary over time, as the focus may shift among issues, particularly because governance reforms may be addressed through legislative and regulatory processes. Themes in governance engagement generally relate to accountability, high ethical standards, sustainability, and alignment of the company and management with the interests of its shareholders and stakeholders. Recent engagements include:

- ❖ **Separation of Chair and CEO:** Independence of the board is important to ensure that the board is fulfilling its responsibility to monitor and assess corporate management performance. A board chair who is also the company CEO may create a conflict of interest in fulfilling these two distinct roles; a board with an independent chair is more likely to act independently and monitor management more effectively. An independent board chair can also improve focus on important ethical and governance matters and strengthen accountability to shareholders. Separation of board chair and CEO is common in many countries outside the U.S., and research in 2009 reported that approximately 79% of United Kingdom companies have independent chairs, while only 43% in the U.S. have separated the roles. In addition, since both are critical corporate roles, a separate chair allows the CEO to focus on managing the company and attending to the relationship of the company with its numerous stakeholders.

- ❖ **Inclusive board membership**: In an increasingly complex global marketplace, the ability of a corporation board to utilize a mix of director attributes, experiences, diverse perspectives and skill sets are essential for a well-functioning board in carrying out its many responsibilities to represent the interests of shareholders and stakeholders. Diversity also increases the likelihood of implementing the right strategic decisions, contributes to a more positive reputation and enhances efforts to recruit, retain and promote diverse, high-performing staff. While many boards focus on experiences and skill sets, there are some that do not appropriately achieve diversity in underrepresented groups in membership on the board, such as women, African-American, Asian and/or Hispanic persons. For example, while women make up more than half the U.S. population, a recent report states that they make up less than 20% of board positions at Fortune 100 companies. Consequently, it is important that a company not only have both a policy supporting board inclusiveness, but also demonstrates its commitment through actual diversity in its board membership. Resolutions have been filed with companies with underrepresentation seeking changes in both board policy and their nominating practices.

- ❖ **Executive compensation**: According to an Associated Press survey of S&P 500 firms, in 2007 average CEO pay rose 2.6 percent to \$10,544,470, which is 344 times the pay of an average American worker. The gap between CEOs and minimum wage workers is even wider, and CEO pay is 866 times that of minimum wage employees. If the increase in minimum wage had kept pace with CEO compensation, it would be more than \$20, rather than the \$7.25 that it is today. It has also been reported that executive pay rose 163% from 1989 to 2007, while the wages of the average worker rose only 10% during that same time. This disparity in compensation is a matter of social justice. Excessive compensation has become a widespread problem, angering shareholders, regulators and the public. Concern with executive compensation practices are not just with the amount, but also their design, which may reward the wrong behaviors. Executive compensation practices need to be aligned with the interests of shareholders and the long-term performance of the corporation and be designed so that both prosperity and downside risks are shared by executives and shareholders alike. Compensation programs should also be transparent and be tied tightly to corporate performance. Recent shareholder initiatives have focused on giving shareholders an advisory vote to endorse the compensation packages of senior executives, and more than 70 corporations have now agreed to give shareholders this right in annual proxies. Other efforts have focused on “pay and benefit disparity,” asking boards to evaluate the overall reasonableness of pay and benefit packages of executives and other company employees and report findings to shareholders.