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ecoDa's Reaction to the British Academy report *Principles for Purposeful Business*

The Future of the Corporation programme is conducted by the British Academy, the UK's national academy for the humanities and social sciences.

In November last year, the British Academy (BA) published a report titled *Principles for Purposeful Business* discussing the concept of the purpose of a company and governing companies accordingly. The report was released against the backdrop of mounting expectations on companies to not only advance the interests of their members/shareholders but also to contribute positively to the fulfilment of urgent societal goals. The report is the second in a two-part series issued as part of the Academy's research programme examining *The Future of the Corporation* and aims at setting out a pathway for realising the ambitious ideas and proposals put forth in the first report.

The report presents a comprehensive and well-conceived framework for achieving this aim. The framework offers bold and thought-provoking ideas about how to better align the interests of privately owned companies with the need to address various social, political and environmental challenges. After revisiting the first report's discussion of *corporate purpose* and introducing the concept of "purposeful business", it proceeds to propose eight key principles for bringing about societal change. The report then goes on to conclude by describing the way in which five "change pathways" could cumulatively result in a paradigm shift.

Beneath ecoDa offers some comments in response to the report with a view to enhancing the important debate on the future of Corporate Governance.

- Our *first* - and most crucial – observation concerns the very concept of corporate purpose, which throughout the report appears seen as potentially incorporating a range of different stakeholder interests *except* that of generating profit for the shareholders. In addition, the heading "Purpose before profit" of the first main section of the report (see p. 10) seems to involve a distinction between the two concepts to the effect that one cannot be part of the other[1].

[1] This is further underpinned by the reference (on the same page) to profit as "a product of a corporation's purpose, but not the purpose of the corporation", a view that then appears consistently underlying the ensuing reasoning. True enough, it is also stated, in slightly varying wordings, that the purpose of companies is to "*profitably* (our italization) solve problems of

However, ecoDa can see no inherent conflict between purpose and profit in practice. Whilst the notion of articulating a corporate purpose beyond realising a profit is well-established it remains important to acknowledge that companies must be profitable even if only as a means to realise another objective. That is to say, companies cannot be good for society if they are going bankrupt.

In order to operate, companies must take the interests of many other parties into careful regard, particularly the interests of employees, customers, suppliers, creditors and other direct business partners. Increasingly, companies must also take account of their impact on society at large. Due regard for a range of such "stakeholder interests" has long underpinned companies' social "licence to operate". In recent years, the number of issues that have an effect on this licence has expanded to include issues such as corruption, human rights violations, environmental pollution and climate change.

We are also surprised to see corporate purpose defined as a set of *means* by which companies may contribute to the solution of various societal problems (p. 16, first paragraph) rather than as its *aim* to do so. ecoDa understands the original purpose of a company to be equated with the reasons why it was first established by its founders, which subsequently evolves over time in line with the motives for of its current shareholders to own and operate the company. This may or may not be to create value for the shareholders (which is, however, typically a key aim of listed companies) but includes for well-managed companies also due regard of the interests of a range of other relevant stakeholders. Hence, by defining and articulating its purpose, the company can disclose its ambitions in those respects to the outside world. Some jurisdictions already today require companies to do so in their Articles of Association (usually with profit generation as the default alternative), and ecoDa would support a dissemination of similar practices throughout the EU.

- Our *second* observation regards the question of how and by whom the purpose of a company is to be decided. Although the section *Defining a company's purpose* (p. 17) is somewhat vague, the report as a whole is clearly based on the notion that this power should rest with the board. This is evident e.g. from a proposed corporate law provision to the effect that "directors of companies must establish their company purposes…" (p. 20, 4th paragraph), and the approval of a similar provision in the new UK Corporate Governance Code (p. 23, 2nd and 3rd paragraphs). The report fails to mention the role shareholders would have in this process.[2]

ecoDa is of a different view. It would entail a far-reaching transfer of power over the company from its members/owners to the board that would in turn constitute an effective reversal of the last half-

people and planet" without, however, on any account referring to profit-making as a major driving force of companies or to the shareholders as its beneficiaries.

[2] The intention appears to be to have companies seek to obtain a shareholder base that is supportive of their (presumably predetermined) purpose, thus achieving the "stability in ownership required to fulfil their purpose" (see Figure 3 and comments, p. 19). In other words, contrary to the current general practice of having the shareholders determine the purpose and then appoint a board committed to realising this purpose, it is proposed to have the board decide on the purpose and then try to recruit shareholders that support this purpose.

century of corporate governance achievements. Modern corporate governance emerged in the late 1970s as a reaction of shareholders to the abuse of powers of undisciplined and self-interested boards and has since brought about a significant and well-motivated return of powers to the shareholders. Delegating to the board to determine the company's purpose would in one go reverse this development and largely strip the owners of the control of their company. The board does not own the company.

Instead the prerogative to determine the company's purpose must remain with its owners.

- Our *third* observation concerns how to hold board directors to account towards a range of stakeholders with in all likelihood different and more or less mutually conflicting interests. The possibility to hold directors legally accountable for the discharge of their fiduciary duties to the shareholders is a cornerstone of effective governance of companies. To have such accountability applying to a wider circle of interested parties, as proposed in the last paragraph of page 23, would in practice risk watering down the directors' fiduciary accountability to their principals: there is a danger that a board held to account for poor performance of the company in terms of certain interests could always point to having opted to prioritise other interests. This, in turn, would risk turning companies into ungovernable entities with serious repercussions on the functioning of the market economy.

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Link to the report

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About the European Confederation of Directors Associations

The European Confederation of Directors Associations (ecoDa) is a not-for-profit association founded in December 2004 under the laws of Belgium. Through its 22 national institutes of directors (the main national institutes existing in Europe), ecoDa represents approximately 55,000 board directors from across the EU. ecoDa's member organizations represent board directors from the largest public companies to the smallest private firms, both listed and un-listed.

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