SPEECH BY DAME INGA BEALE

Putting Theory Into Practice : Boardroom Governance For Real

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Corporate accountability – what has happened to corporate accountability? What happens to board directors after a company has failed? Do we have the right approach to Corporate Governance and responsibility or does there need to be a major re-think?

In the run-up to the global financial crisis, it was financial engineering that helped drive a frenzy of reckless risk taking. So, when Lehman Brothers collapsed, and Christine Lagarde famously challenged whether the same failings would have happened if it had been Lehman Sisters, we were left wondering if corporate governance was actually working as intended. Policymakers were facing what could be referred to as a “holy cow” moment”.

The most striking thing for all of us back then was the incredible fragility of so many large financial institutions. At their very core, these firms had been weakened by inadequate equity capital, flawed business models, and the blindness of powerful men – a toxic combination that left taxpayers on the hook for massive bank bailouts.

Here in the UK last month we saw the collapse of a travel company – Thomas Cook – the oldest travel company in the world. It is not material enough and certainly not interconnected enough to spark a global financial crisis – far from – but it got lots of dramatic headlines such as : the government launches the largest repatriation in peacetime history.

Operation Matterhorn was launched and about 700 flights were organised by the Civil Aviation Authority to bring back the 150,000 or so stranded passengers.

The collapse has brought the accountability and responsibility of the board – and of the auditors – right into the spotlight again.

It is such a fresh collapse that the government enquiry has only just started but the board directors will all be questioned and challenged. The emotive thing for the general public is the loss of jobs for thousands of people and the high level of compensation paid to the CEO and other executives.

Last month also saw a lot of commentary 21 months after the collapse of Carillion – a UK firm that was put into compulsory liquidation with liabilities of £7bn and of course it gets the public attention because thousands of workers lost their jobs. No action has been taken against the company's directors or senior managers responsible for its collapse and the Official Regulator is still undertaking an investigation into whether there was any criminal wrongdoing by Carillion's directors prior to the company's collapse.

The investigation is not expected to complete until early 2021 and in the meantime all the directors are free to pursue new lucrative roles while the innocent workers have a long battle ahead of them in their battle to secure compensation.

It would appear from what has been reported to date that the non-executive directors asked insufficiently probing questions on the financials.

There was an enquiry done by two government committees who said in their findings that "Carillion's rise and spectacular fall was a story of recklessness, hubris (self-confidence) and greed", and that even as the company collapsed, its directors were only concerned with protecting their "generous executive bonuses".

The report described the culture at Carillion as "rotten", and claimed that internal and external checks and balances that could have prevented its failure were completely absent.

The committees recommended to the Insolvency Service that it considers whether these directors were in breach of the Companies Act, meaning they could face disqualification from future director duties.

Furthermore, Carillion's non-executive directors "failed to scrutinise or challenge reckless executives".

There are many people asking that if a company fails isn't the board responsible? They are asking that maybe the board members of a failed business should be stopped from being board directors again.

Now this brings up many other questions as how this would work for instance if you need to appoint someone onto a board for a turnaround that may or may not work. And presumably going into an orderly administration might be considered OK while collapsing straight into liquidation is not appropriate.

Another question arises a lot these days and that is about whether over-boarding contributes to poor corporate governance. Should there be limits as to how many directorships an individual can have.

As a CEO I saw great benefit of using my NEDs to be real buddies for some of my executive team. Those who were digital experts spent a lot of one on one time with my Chief Operating Officer who was driving through a massive transformation programme. They were able to do deep dives and provide in depth guidance to the executive as well as provide more rich contributions and challenge round the board table. It gave them the additional context to understand and get under the surface of issues.

But if your NEDs are on too many boards how would they have the capacity to spend all this extra time with the executives. And perhaps they would feel that they're not being compensated enough to do that.

I believe that regular interaction between NEDs and executives is very helpful and prevents the Board from being too remote. Although it is still vitally important to get the balance right between being a "friend" of the executives vs looking out for the shareholder and employees' interests.

Thinking about Christine Lagarde's "sisters" comments regarding Lehmann Brothers, there was one female NED on the Carillion board and three on the Thomas Cook board so, as usual, there is no hard and fast rule for any of these things.

And I'll let you, the experts, delve more into why the corporate governance seems to fail so dramatically in some instances.

Instead, I'm going to move on to explore some of the many topics that also take up a lot of Board time and will give a flavour as to the complexity of getting the governance right these days.

Right now, across the world; society, business and governments are confronted with enormous change and challenges, all of which present risks – both new and old.

I'm from the world of insurance so watching and assessing risk is our business. But we're struggling to get our arms around any one of these risks in isolation – so how are we going to get our arms around them all? There is no silver bullet. But what is certain is that complacency, ignorance – or worst of all flat denial – is not the answer and I believe that Boards need to be considering all of these things.

Today I shall share some views on the big challenges that the world is facing. This is by no means an exhaustive list but these are the topics that are high up on the priority risk list as I see them.

First I'll touch on the geo-political environment and the huge uncertainty all around us. Then I'll talk about technology and business model disruption. A really big hot topic will be sustainability and climate change and I will also talk about stakeholder engagement activities and the push from more and more campaigners and activists to force governance changes to address diversity and trust.

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Globalisation and increasing digital connectivity have inarguably brought the world closer together. International trade has helped drive economic growth and lifted many millions out of poverty. Exports of goods and capital have increased the growing wealth of nations around the world.

Every country in the world relies on this international network of trade partners and political allies who support economic opportunity, collectively and collaboratively. But if globalisation has brought so many benefits, why have we reached the point where retrenchment and national self-interest have become such a big threat to international stability?

The proponents of globalisation are losing ground. Around the world people are rallying against the status quo – whether they are unhappy with business, government or media – they're demanding change and a better future, a future that puts people, rather than profit, first.

Some of that has been the reason for the outcome of the EU referendum here in the UK in 2016. Now, over three years later the government is still trying to negotiate for the UK to leave the EU. Tensions remain very high between the various different groups of people in the country – particularly those who want to leave and those who want to remain.

For some sectors Brexit still contains a lot of uncertainty as regards how trade will be handled between the UK and the EU. Coming from the financial services sector things are rather different as services are not usually part of trade agreements. It is simply a matter for insurers and banks of losing their licenses to do business in the EU 27 states.

In the Boardroom I sat in, Brexit became almost all consuming. As a CEO in 2017 I was spending 30% of my time on Brexit and we probably spent about 20% of the Board time on the topic. That meant that there was no bandwidth to handle anything new and basically investment into projects and new initiatives came to a standstill with the exception of some key initiatives that were already in train.

I know from conversations with many other CEOs that they were experiencing the same. We fundamentally lost time and had to focus on executing on plans to set up operations and gain trading licences elsewhere in the EU just so that we can keep serving customers as before.

A lot of the pressure came from regulators who were demanding that we take action to ensure we had viable going concerns. The Brexit defensive action has added a lot of additional cost to business and billions in reserves and capital has been transferred out of the UK into other countries within the EU.

I find it fascinating, but also depressing, that some of the economies that have thrived thanks to this global network of trade and capital, believe retreating to protectionism is the answer. It is not.

I believe we all must continue to make the argument for the benefits of economic connectivity, while striving to ensure those benefits are more widely shared.

Now onto technology … technology is shaking the foundation on which our traditional business models are based, and it is posing new risks all around us.

The threat to personal data and the threat to all of us as individuals, and as representing business, is all a result of the digital revolution – the 4th industrial revolution, which has had a profound impact on the way we communicate and do business. It has been going on since the personal computer was first invented, when information began its evolution from the physical world of books and publications, to the universal language of computers.

We live in a world that, if you're not paying for it, you're the product. What I mean by that is that everything we do on our phones or computers captures something about us in data form. Your age, location, interests, leisure pastimes, spending habits, and even your political leanings are all valuable data points for companies, app providers and social media platforms.

All of these organisations should be needing to prove that they are behaving responsibly with the masses of data they are collecting – and that they are protecting it from those that are out to misuse it.

And this is just one of the consequences of our digital world and the huge advancements we are seeing in technologies. The insurance sector, is right up there with businesses that need to show they are behaving responsibly with the masses of data we are collecting, the use of machine learning, the use of algorithms and artificial intelligence.

The rise of artificial intelligence is driven by exponential increases in computing power and by the availability of vast amounts of data. In 2018 alone more data was created than in the entire history of the human race. So when we describe an exponential increase in the amount of data, it's real.

With this explosion in the amount of data and the number of devices come consequences that we hadn't previously thought about. There is already a lot of discussion about AI using biased programming and data selection, which could lead to all sorts of class actions in the future unless we start taking the concerns seriously and re-think who and how we will programme and test the AI.

There is a wonderful book to read by Caroline Criado Perez called "Invisible Women" in which she has assembled a cornucopia of statistics with a focus on gender bias. She talks about it being a man's world because those who built it didn't take gender differences into account. For instance women in Britain are 50% more likely to be misdiagnosed following a heart attack as heart failure trials generally use male participants. Cars are designed around the body of "Reference Man", so although men are more likely to crash, women involved in collisions are nearly 50% more likely to be seriously hurt.

Gender-blindness in the tech culture is something we really need to take seriously as many firms are using AI to refine our product offerings.

One woman reported that her car's voice-command system only listened to her husband, even when he was sitting in the passenger seat!

Even snow-ploughing, it turns out, is a feminist issue: in Sweden, roads were once cleared before pavements, a policy derived from data that prioritised commuters in cars over pedestrians ferrying children or doing the shopping. But then officials realised that it's easier to drive through three inches of snow than push a buggy through it. Clearing pavements first also saved the state money: a study in one Swedish town found that pedestrians were three times more likely to be injured in icy conditions than car drivers; and 70% of those injured were women.

Any Board that wants to do the right thing should be ensuring that any programming and use of data is being done fairly otherwise there could be huge reputation damage.

According to recent BCG research, the biggest perceived technology challenge to business is a lack of qualified employees. Digitally talented people are already so highly in demand that many large, traditional companies must reinvent themselves to attract them.

So businesses have to work hard at attracting new talent and seeing that many businesses these days describe themselves as a tech company or will shortly become a tech company, there needs to be a push from the Board to ensure that the culture is moving in the right direction.

When recruiting in new tech savvy talent you have to understand these digital employees and most importantly understand how digital employees think.

There does seem to be a kind of digital mindset.

Employees with this mindset are entrepreneurial and inclined to data-driven decision making. They focus on user-centric product and service development and are passionate about creating and building. They are experienced in and like to work in collaborative teams and in agile ways of working.

When it comes to the work environment, digital employees are more concerned about what they're working on and what they're building than about prestigious titles or linear career paths.

They want to be surrounded by inspiring peers and thought leaders in their field of expertise. Many also want to make a meaningful, positive impact on the world, and most would like to define their own work-life balance.

So to create a truly digital culture, the organization needs to introduce and adapt to new forms of cooperation, implementing more project-based work and running these projects in a more flexible way. Not something that many huge companies that have been around a long time are good at.

But new working methods such as agile and user-centric product design, along with more experimentation and creativity, fewer fixed rules, and more tolerance for risk taking, are essential. Digitally savvy employees tend to be fast learners who crave responsibility and impact, but they will make mistakes; so a culture that accepts failure is essential.

As a leader, people watch more closely what you do than listen to what you say, so make sure you really model the new values and behaviours that you want to implement. If you want to demonstrate that failure is OK, then get out there and reward it!

And that means helping those in the boardroom understand that it's OK to make mistakes – not something that is traditionally tolerated.

But there are other things changing in the boardroom driven by the digital revolution we're undergoing and that's the cyber threat that's out there.

Cyber-attacks are starting to take their toll on global economic development. It could cost the global economy 6 trillion dollars per year by 2021, according to Forbes. In 2017 there were almost 1 billion global victims of cybercrime, stealing 150 billion euros from consumers.

A British expert in criminology from the University of Surrey estimated that the cost in 2018 had already reached 1.5 trillion dollars.

The profits from which will be larger than any other illicit trade that drives the shadow economy such as the profit from trading major illegal drugs.

But the fallout is not purely financial.

For businesses there are other serious consequences of cyber- crime including reputational damage, the loss of investor confidence, a loss of management focus and the sacking of key executives.

As insurers we grew up insuring and protecting physical risks – a building, a port, a ship, a cargo, an aircraft, a major construction project. In the 20th century we started to insure liabilities so the world of intangible risks started to grow. Intangible risks have grown so much that today some of the most valuable companies have built their success not by owning physical assets but by creating intangible assets such as software and algorithms that collect data and they use it to deliver and constantly refine services.

But while I personally love how technology is revolutionising how we live and work, cyber-crime is undoubtedly the dark underbelly of the digital revolution. And we need to confront it head on and not stick our heads in the sand and hope it will go away.

Quite understandably there is a nervousness around cybersecurity that pervades throughout organisations. And the boardroom is no exception. It is being discussed more and more in the boardroom and board members can't escape having to have a basic knowledge of how technology will transform things. They also need to understand how technology opens up a huge cyber vulnerability because tech touches everything.

There can also be some defensiveness from executives when responding to questions from Board members when actually they are just wanting to learn and understand the issues so that they feel they can add value.

What I would recommend for a board to do right now is unless you have a genuine interest in the technical workings, and there will be some board members who do, the rest do not need to worry about gaining a deep understanding of how machine learning, AI, RPA, blockchain, and other cognitive technologies operate.

Instead, they need to understand how the technology makes the organisation more vulnerable.

The questions they need to ask are how vulnerable is the organisation to a cyber-attack? What mitigations are being put in place? What actions are being taken around cyber security?

Briefings from management should focus on benchmarking and independent reviews and assessments. Boards always love to have someone from the outside come and check how things are in the company and there is no need for management to feel defensive about this or think that they know better and an independent body can't add anything.

The board will want to see that business continuity planning exercises are being carried out by the business so that they are drilled in knowing how to respond should there be an attack. The immediate response in that crisis moment is critical in terms of how the company will fair.

Practice, practice, practice – just like is done on the sports field.

Coming from the risk business I am used to dealing and quantifying risk. If a Board does not have a strong focus on risk I would be worried. Risk management should be seen as a kind of shadow entity that sits beside everything a company does.

Just as we need marketing to look after customers, finance to look after money, and human resources to look after people; we need a risk leader to look after this strange entity of risk.

In the absence of a risk leader, no one else has the time, inclination or skill set to develop a holistic view of risk and how to manage it.

Ideally, within organisations there should be some separation between operational and strategic risks and it's the operational side that really needs to focus on the new risks that digitalisation brings.

And now onto the main challenge that we all face – climate change and the climate crisis that we're now in. Certainly not an issue that will go away if we don't do something about it.

There is no bigger story than climate change and the threat it poses to life on Earth. Despite this, there is still a lack of agreement on the topic and the media have certainly not helped.

In newspapers and online, media outlets have often given platforms to writers whose political leanings – writers who have had less than rigorous engagement with the science – and have therefore been able to influence others' outlooks on climate change. And that's only considering the times climate change has made the news at all.

Even in 2019, as experts warn we have vanishingly little time to divert catastrophe, major TV networks in the US dedicated more coverage to Britain's royal baby during one week in May than they had to climate change over the whole year up to that point.

From an insurance point of view, we see the full force of the impact of the climate crisis with extreme hurricanes sweeping across the Atlantic. We see flooding in Asia, and wildfires in Europe and the US.

The 1st of June marks the start of what we call the Atlantic Hurricane Season. The season peaks on the 10th of September and officially finishes on the 30th of November. The Hurricane Season takes place every year and its costs vary each year in terms of loss of life and economic impact. Each year, once a storm has been registered as exceeding a certain windspeed, it gets an official name that is used throughout the world.

The World Meteorological Organization is responsible for developing the names for the Atlantic storms. They use six lists of names and these lists rotate each year. That means every six years, the names cycle back around and get reused. If a hurricane does tremendous damage, such as Katrina, Sandy, or Harvey, the name is retired and replaced by a different name beginning with the same letter.

The names alternate between male and female names, and they are listed alphabetically and in chronological order starting with A.

In this year's hurricane season we are already at "M" – Melissa – with the most devastating one so far this year being "D" – Dorian – which tore through the Bahamas last month and was the most intense tropical cyclone on record to strike the island. It then hit the east coast of the US and Canada and even touched Greenland. The latest death toll is now 70, a huge number of people were displaced, and the economic hit is large.

In another part of the world these storms are called typhoons and their names are determined by the Japanese Meteorological Agency. Unlike the hurricane list there is one list with 140 names on it and the names are simply rotated and have no time restriction on them. In other words, a new list is not started each year.

The latest typhoon there is Hagibis and is getting perhaps much more attention in the UK than is usual as it is disrupting the World Rugby championships that are taking place in Japan. Some of the matches are being completely cancelled – including the England match – and they are then treated as draws for points purposes. The points being a vital part of whether or not a team will qualify for the next round.

We can't say definitively if climate change increases the number of hurricanes and typhoons, but it does make them more powerful and destructive and cancellation of sporting events puts the topic much more in the public eye. Higher sea temperatures mean stronger winds and more rain for hurricanes to dump. Rising sea levels mean a greater risk from storm surges and from coastal flooding.

In 2017 a new record was set: we saw the longest list of consecutive named storms to achieve hurricane severity since 1893. The weather is getting worse and more damaging, something the insurance industry is clearly concerned about. Over the past two decades, the impact of total global damages from climate related events rose by more than 11 percent per year – to more than 300 billion dollars in 2017.

2018 was a more benign year for natural disasters but the cost was still huge at 160 billion dollars.

The numbers are staggering because in addition to the economic cost there is a tremendous human cost. 100 million people are at risk of being pushed into poverty by climate change by 2030; particularly in other areas not necessarily impacted by hurricanes like sub Saharan Africa and South Asia.

So the question is: what can we do? What can Boards do? What will they have to do? In the UK the Financial Reporting Council, the FRC, has laid out their expectations for boards in relation to climate change.

Boards have to consider the company's impact on the environment and address and, where relevant, report on the effects of climate change both direct and indirect. However, compliance rates with these reporting requirements remain low which calls into question how seriously the Boards are taking this crisis.

But we have to think differently and climate change must be on every board's agenda in some form or other.

In an age of increasing focus on sustainability, for those involved in the construction sector, it is too short-termist to simply keep replacing what is damaged in severe weather events rather than getting on the front foot through prevention and 'building back better'.

Building back better is making sure that when homes, communities and businesses are rebuilt, they have greater resilience to future events by integrating disaster risk reduction measures as they are replaced.

More widely, it also enables governments and communities to scale up climate adaptation efforts to ensure more efficient planning. Investing in prevention not only improves resilience, it also safeguards economic growth and other development achievements from being wiped out.

According to the UN, for every £1 spent in prevention, around £7 will be saved when the worst happens again. However, that extra pound or dollar has to come from somewhere and if forward planning pushes the price of insurance to a level that customers won't pay, then where does the responsibility for this lie? With the industry? The regulators? The government? The answer is: all of us. We must take collective responsibility across everything we do.

This includes integrating climate risk into our view of the economic outlook, investing in lower carbon infrastructure, putting a price on carbon, active stewardship on climate risk and where necessary divestment from companies whose environmental philosophies are opposed to our own.

This would stimulate companies to adapt their strategies towards sustainability, ultimately helping create a world that is good for business, people and the planet. There isn't one single action that will reverse climate change, but working and living sustainably is the long-term solution to it.

And responsibility lies with individuals and businesses alike. So we all need to constantly ask ourselves how we can make sure that what we build is truly better and not simply a short-term fix, as it is safe to assume that a future hurricane season will set a new record of its own.

Extinction Rebellion is a call out from the young generation and some of the older generation too that we must take action. They are calling out to businesses to take responsibility for their actions of the past and do things differently in the future. They do not believe we are taking the matter seriously and they could be right.

They could be right not to trust big business on this topic which this brings me onto another challenge – the trust deficit – something that I find deeply worrying.

There is something lurking beneath the events we have seen both here in the UK, with the vote to leave the EU, and with other events around the world over the past couple of years. People simply don't know who to trust anymore.

The annual Edelman trust barometer which tracks levels of public trust across the globe shows that the public have low levels of trust across government, media, business and even NGOs.

But how has this happened? How has public trust – hard won and so easily lost – eroded to the point that we are now seeing?

The fact is that people don’t trust society is working for the majority. And who can blame them when you consider that 70% of the world’s population holds just 3% of global wealth. In fact the world’s wealthiest individuals, who make up just 8.6% of the global population, own nearly 86% of global wealth. Those numbers are really quite shocking.

Now it’s not all doom and gloom as there has been real progress in reducing poverty over the past decades and since 2000 when 27% of the world population lived in poverty, we are now down to less than 10%. However, it’s the distribution of wealth that is still somewhat alarming. Oxfam reported that last year the 26 richest people on earth had the same net worth as the poorest half of the world’s population, some 3.8 billion people.

So in this world of inequality we can understand that people are not trusting that society is working for the majority of us. A reset is needed: to win back the public’s trust, and create a more effective system fit for our 21st century society.

So how do we restore the public’s trust?

Business leaders in particular have a role to play that they have not perhaps felt the need for, or indeed desired, in the past. They need to step up and talk openly on topics that society wants to see more leadership on. One of those topics is the purpose of the Corporation.

The “goal” of a corporation cannot be just about its own narrow financial interest. It must also encompass a broader common responsibility.

It is not surprising, therefore, to see growing debates about the nature of modern corporations and the concept of maximizing shareholder value.

As the British economist Colin Mayer put it: “For nearly all of its 2,000-year history, the corporation has combined a public purpose with its commercial activities. It is only over the last 60 years that the idea that profit is the only purpose of business has emerged.”

I believe that encouraging a broader common responsibility is now more important than ever – not just for today’s stakeholders, but for future generations.

We can see there are groups starting to talk seriously about it. Some groups of academics, like the work lead by Professor Colin Mayer at the British Academy, have been working on this topic for years.

And of course not so long ago we read the Business Roundtable’s, the BRT’s, new “Statement on the Purpose of a Corporation”.

However, I sense there is quite a bit of cynicism around. Nearly ten years ago the same group released a report title “Enhancing our commitment to a Sustainable Future”. Does it feel as though anything changed off the back of that? Perhaps not.

If businesses really want to have the public trust them again, they have got to mean what they say and act on it.

Can you act on it through your CSR programme?

Is it good enough to pay for carbon offsets so that your environmental ranking improves? Is it good enough to have lots of words saying the right thing on your website about your approach to modern slavery?

Perhaps not ...

I have a personal story I would like to share with you about a friend who has become a hero of mine and role model – Afroz Shah, a lawyer based in Mumbai in India.

[PERSONAL STORY OF AFROZ SHAH SAVING THE OCEAN FROM PLASTIC]

It’s not good enough to throw money at it, it’s got to have genuine social impact and so I am all for scrapping CSR programmes. Not because I want business to stop doing the right thing or have people lose their jobs if they work in those teams. But because I believe the entire organisation needs to be built around being sustainable.

The values and the purpose of a business, have to have the interest of a wider group of stakeholders at their core. There has to be value to society built into the main business of a company, not as a side-line or under a CSR programme. I want CSR to be at the very heart of what a business does. I really believe that we have to change the purpose of the Corporation – and quickly.

Now I believe that inclusion is going to be the key to solving this. This one word encapsulates society's plea to have a louder voice, to be thought about, and to be involved.

When you boil it down, this is all about inclusion.

I have been passionate for a long time about the need for inclusion – I know how I felt when I was fighting in a man's world back in the 80's when I first started my professional career.

But now it's imperative that businesses play a huge role when it comes to driving societal change and business leaders need to lead on the inclusion agenda. And – leaders must be authentic on the topic as people can see through the "blah blah" words.

Employees expect it. Customers expect it.

We all know from the reports that are published that the performance of firms who have diverse leadership teams is improved. We know that the most innovative teams are those that have diversity in them and that it is essential when you're going into a new market you need to have diverse teams. Diversity in all its form has a positive impact for business.

This is where the Board can really lead from the top. A Board can place demands on its executives to do things differently. To reward and recognise a different type of behaviour. To set targets and ensure there are repercussions for not achieving those targets.

To sum up, there is clearly a lot on the Board agenda and governance is being more and more closely looked at by investors and regulators alike.

It is essential that the Board considers its wide range of stakeholders – its customers, its employees, its shareholders. But I feel that by prioritising one over the others will not work in the long term. There needs to be more balance and we must make sure we listen to all the voices.

Inclusion is the way to build prosperity for all. We can drive this from the top of organisations and have a broader positive impact on society. Let's see what we can all do in a small or large way to embrace inclusion and reverse the trust deficit we have in society through thoughtful and considerate corporate governance.