

## **Traidcraft demonstrates the Corporate Responsibility Coalition's objectives and proposed Company Law Reform Bill amendments are not only operational but also good for business**

### **1. Traidcraft**

Traidcraft is the UK's leading fair trade organisation, selling food, household products, soft furnishings and clothing from nearly 100 producer groups based in 31 countries in Africa, Asia and Latin America. Traidcraft was established in 1979 and is comprised of two operational organisations: Traidcraft plc and Traidcraft Exchange, a registered charity. Both parts of Traidcraft have the same mission statement of 'fighting poverty through trade.'

#### ***1.1. Traidcraft Exchange***

Traidcraft Exchange is a development charity whose work spans capacity building amongst producers in developing countries, market access, policy development and advocacy. Through its Policy Unit, Traidcraft Exchange, in conjunction with developing country partners, seeks to influence government policy and business practice in the North and the South to the benefit of the poor in the developing world.

#### ***1.2 Traidcraft plc***

Traidcraft plc is a medium-sized company, with a turnover in 2004/5 of £15.5 million and a profit after tax of £384,000. Traidcraft plc raised £3.25 million in a successful share issue in 2002. Traidcraft plc buys products from agricultural, craft and textile suppliers on fair trade terms and sells these products through a variety of channels in the UK. Traidcraft plc has 105 employees and 5750 shareholders following the share issue in autumn 2002. Traidcraft plc's purpose is to be a model fair trade company and thereby influence other companies as well as having a direct impact itself. Any profit goes back into the business or is paid out in dividends close to the level of inflation. Traidcraft also sets aside additional funding to go into discretionary producer support activity where profitability allows.

### **2. Comparing Traidcraft plc against the three Corporate Responsibility Coalition goals for changes to the Company Law Reform Bill**

The three aspects of corporate accountability CORE is promoting include:

- directors are legally obliged to minimise any damage their company does to local communities and the environment;
- companies are legally required to report on their social and environmental impacts;
- people overseas who are harmed by the activities of a UK company are able to take action against them in a UK court.

#### **A Directors are legally obliged to minimise any damage their company does to local communities and the environment.**

##### ***2A.1 Duties of Traidcraft plc's Directors***

Traidcraft's board of directors follows good corporate governance as set out in the Combined Code. In addition, Traidcraft's directors act in accordance with Traidcraft's Memorandum, Articles of Association and Deed of Covenant (which cover Traidcraft Foundation, Traidcraft plc and Traidcraft Exchange). These require the directors to consider social and ethical factors as well as profits and income in the running of Traidcraft plc. Obligations set out in Traidcraft's structure include:

- ensuring that stakeholder views are represented in company deliberations and planning processes;
- a requirement that Traidcraft remains accountable, transparent and true to its mission, fighting poverty through trade, by ensuring that social accounts are produced each year. Traidcraft's social report, called Social Accounts, are seen as a core part of Traidcraft plc's governance;
- to respect all people and the environment;
- to abide by and promote fair business practices;
- a requirement for additional checking and discussion if a dividend in excess of 2.5% over the RPI (Retail Price Index) inflation rate was proposed.

Traidcraft's 27 years of operating as a successful social business prove that it is possible for a company board of directors to consider and balance diverse objectives (e.g. financial, ethical and social) when coming to a decision.

### **2A.2 Current and proposed legal requirement approach to Director's duties**

The current and proposed legal requirement (in the Company Law Reform Bill) is for directors to continue to act in the best interests of their members (ie shareholders) as their top priority. (The draft wording is for directors to act in a way which 'promote[s] the success of the company for the benefit of its members as a whole.')

Employee, community, environmental and business relationships with suppliers, customers and others only need to be considered if they are important to shareholder value, rather than considered with the objective of minimising harm or realising international human rights standards.

### **2A.3 Cost/Benefit of Traidcraft's approach**

Traidcraft plc benefits from directors considering wider issues than purely financial considerations in its governance. This approach enables Traidcraft to have more constructive relationships with its suppliers, customers, employees and shareholders than companies whose main driver is purely profit-maximisation. This has been demonstrated by Traidcraft's ability to raise £3million capital.

In particular, Traidcraft considers that it gains the following benefits from the closer consideration of stakeholder interests and consultation/feedback processes with stakeholder groups:

- increased awareness of the priorities of developing world suppliers, enabling Traidcraft to work with them to strengthen our supply chains – to mutual advantage;
- increased loyalty from customers/supporters/shareholders who value being consulted;
- Traidcraft is better attuned to customer/supporter trends and concerns, and so able to adjust its activities and communication priorities to ensure continued support;
- transparency and consultation leads to increased sense of partnership with UK suppliers, leading to identification of more constructive collaboration opportunities;
- better identification of staff attitudes and concerns, allowing Traidcraft to respond to any emerging issues at an early stage and maximise morale and motivation;
- better identification of issues that need to be addressed, but have not previously been prioritised by Traidcraft (e.g. environmental impact of the business).

## **B. Companies are legally required to report on their social and environmental impacts\_(and the directors are legally required to minimise their negative impacts)**

### **2B.1 Traidcraft plc's social reporting**

In order for Traidcraft's directors to improve the company's social impact, they need to understand and monitor what Traidcraft's social impact is. Traidcraft collects this information through 'Social Accounts'. These involve consulting with stakeholders and feeding those views into Traidcraft's management decision making and reporting. Traidcraft publishes its social accounts in the form of an annual report available in print and on the web. Traidcraft is a pioneer of social accounting in the UK – it published the first independently audited plc report in 1993<sup>1</sup> and recently won the 2005 ACCA award for the best social report.

### **2B.2 Current and proposed legal requirement approach to Director's duties**

Under the proposed new law, companies will be required to produce an annual 'Business Review.' This is a weaker reporting standard than that proposed by the Operating and Financial Review. Both require that employee and environmental impacts of companies only be disclosed if they are likely to impact on shareholder value. OFR also expects the following to be disclosed:

- social and community issues which are material to business;
- main trends and factors underlying a company's current and *future* performance/position;
- use or deviance from a reporting standard;

---

<sup>1</sup> The methodological approach (which Traidcraft developed initially with the New Economics Foundation) has been adopted and adapted by many larger organisations. It has also helped shape the AA1000 standard operated by the Institute of Social and Ethical Accountability (ISEA).

- auditor's statement commenting on whether matters inconsistent with the OFR have come to their attention and whether directors prepared the OFR after due and careful enquiry;
- information about contractual or other arrangements essential to the company.

The OFR places a higher duty of care on directors to exercise 'due and careful enquiry' (rather than the Business Review's 'due care, skill and diligence') when preparing the reports. If companies are not encouraged by law to monitor their impact it remains difficult for them to take steps to improve it.

### **2B.3 Cost/Benefit of Traidcraft's approach**

The Social Accounts measure Traidcraft plc's performance against strategic social and management objectives and gather stakeholder views. Issues that stakeholders highlight as a priority are incorporated into Traidcraft's social accounts' performance measures. Putting in place measurement systems can improve management decision-making and can act as an incentive to influence behaviour.

At board and senior management level Traidcraft plc's Social Accounts are a useful driver and source of information with which to better understand Traidcraft plc's effect on stakeholders, and monitor and improve the way the business is working. In Traidcraft's case, using the social accounting indicators within the company's regular internal reporting mechanisms enables the managers and staff at all levels to balance longer-term social objectives with the need to focus on sales turnover and profitability.

Publishing Traidcraft's shortcomings and areas where targets have not been met reduces vulnerability to external criticism of Traidcraft's integrity, and gives added incentives to ensure that Traidcraft does meet its targets. The production of social accounts costs £25,000 (comprised of staff time and an external audit fee).

### **C People overseas who are harmed by the activities of a UK company are able to take action against them in a UK court when unable to access justice in the country of violation.**

To make corporate accountability real for an affected party there needs to be a mechanism in place so that the affected party is able to raise a concern about the accused company. Complaints need to be lodged with a neutral party, and redress decisions judged by an independent organisation.

CORE is asking the UK government to propose mechanisms, possibly within company law, which would enable a UK company to be held to account by impacted communities abroad. Until those mechanisms are in place, CORE is seeking to strengthen the ability of minority shareholders to hold a company to account through the Company Law Reform Bill.

### **2C.1 Fair Trade system's approach to complaints and redress**

The monitoring and evaluation involved in being a certified fair trade company helps to guarantee against some abuses in the supply chain and provides some protection for producers and communities overseas. Many fair trade companies are also values-based – some have structures in place that enable the producer voice to be heard at Board level and legally binding codes of practice.

However access to redress for producers and communities overseas and the sanctions available are limited both the remit of the fair trade networks and the existence of appropriate international legal frameworks. There is still an important role for government in providing an independent body that can hear complaints from affected parties overseas. Traidcraft supports the introduction of these mechanisms by government.

#### Traidcraft's procedures

Traidcraft has clear internal procedures for handling complaints. Producers/suppliers, customers, employees and shareholders can raise their concerns initially with the relevant Traidcraft member of staff. If they receive insufficient response they are able to raise concerns with senior management, the Chief Executive and ultimately with the Chair of the board of directors. Should these internal channels

fail the impacted party can use two structures within the fair trade system, which are independent of Traidcraft (Fairtrade Foundation and the International Fair Trade Association).

### Fairtrade Foundation<sup>2</sup>

Traidcraft is a licensee of the Fairtrade Foundation (the UK arm of the international Fairtrade Labelling Organisation (FLO)<sup>3</sup>). Licensees are usually companies based in developed countries that pay to put the Fairtrade mark on a Fairtrade product. The Fairtrade Foundation certifies products against agreed international Fairtrade standards – these standards must be conformed to if a company wishes to use the Fairtrade certification mark on its products. The Fairtrade Foundation monitors the producers of the products, ensuring its social and environmental standards have been respected in production. By maintaining a close working dialogue with producer groups, they are able to hear reports from producers about abuses of the Fairtrade system by other actors in the supply chain.

The Foundation also audits the sales of Fairtrade certified products to ensure that licensees of the Fairtrade Mark comply with its standards. If there is a problem of non-compliance with its standards, either by registered producer groups, or by licensees of the Fairtrade Foundation, then a system of corrective action is automatically invoked. This system aims to take a pro-development rather than a sanctions approach – i.e. a party deemed to be non-compliant with Fairtrade standards will have a period of time in which to comply. Ultimately, however, non-compliance risks rejection from the Fairtrade system, and the removal of the right to carry the Fairtrade certification mark.

### International Fair Trade Association<sup>4</sup>

Traidcraft is also subject to the International Fair Trade Association's Internal System of Control. Through this, IFAT members are expected to complete a self-assessment of their performance against Fair Trade standards bi-annually. This report is then critiqued by other IFAT members through peer review and IFAT arranges independent verification of a percentage of members' reports each year. The emphasis is on the participation of stakeholders in the assessment process. Members who have successfully completed this system are entitled to use the IFAT "Fair Trade Organisation" mark in their publicity. This award is at the discretion of IFAT's Executive Committee on the advice of a separate Registration Sub-Committee. Non-compliance with these requirements is a violation of IFAT membership.

In summary, Traidcraft, through its participation in Fairtrade networks, is able to guarantee that a complaint will be investigated and can be heard in a substantive way in an impartial environment. The sanctions of the fair trade movement are either expulsion from IFAT's membership or removal of the right to carry the Fairtrade mark on products.

It is the role of government to design a broader independent approach, which provides affected parties with a legal right to redress.

## **2C.2 Current and proposed legal requirement approach on stakeholder redress**

Only shareholders and the Department for Trade and Industry (DTI) are able to take action against a company director under company law. However, in practice company directors are rarely prosecuted by either shareholders or the DTI for the impact of company actions, partly because of the inherent conflict of interest involved in doing so (loss of shareholder value).

### *Limitations of Enlightened Shareholder Value*

In 2001 Traidcraft put the concept of Enlightened Shareholder Value (currently being proposed by government) to the test by initiating the Just Pensions' Project. The aim of the project was to explore how socially conscious investors could improve the international development impacts of the companies they invest in.

The learning from the Just Pensions' Project was that Enlightened Shareholder Value is insufficient. There are real limitations to shareholders' ability to hold companies to account for their social and

---

<sup>2</sup> [www.fairtrade.org.uk/standards.htm](http://www.fairtrade.org.uk/standards.htm)

<sup>3</sup> [www.fairtrade.net/](http://www.fairtrade.net/)

<sup>4</sup> [www.ifat.org/](http://www.ifat.org/)

environmental impacts and even the existing chains of accountability for financial impact are weak. Learning from Just Pensions indicates:

- directors duties need to include an obligation to consider and minimise social and environmental impacts;
- the obligation on considering social and environmental impacts needs to be incorporated into company law so that it is applicable to both listed and private companies;
- threat of sanctions on directors needs to be stronger.

### ***2C.3 Cost/Benefit of Traidcraft's approach on Corporate Accountability***

The independence of the fair trade system of standard-setting and compliance enforcement enables Traidcraft plc to stand up to criticism and present an honest and transparent case to its customers, shareholders, suppliers and other interested parties.

There is a strong business rationale for the fair trade system to be open to close scrutiny – it is essential that there are mechanisms in place for resolving concerns expressed by any part of a fair trade supply chain for fair trade to be credible.

However whilst the fair trade movement should seek to continuously monitor its supply chains this must be backed up by an independent mechanism introduced by government. It is the role of government to safeguard human rights, deliver on poverty reduction and ensure that if violations are committed by UK companies, an adequate system of redress is in place.