Position paper — workplace health and safety governance

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Management of social, environmental and corporate governance risk is integral to the creation of long term and sustainable shareholder value. Failure to manage social, environmental and corporate governance risk results in sub-optimal business performance. This can be due to community, regulatory and/or litigation liabilities that may arise.

Workplace health and safety (WH&S) has long been a part of business risk management. This has been mandated via state-based WH&S regulations and reporting frameworks.

What is notable in Australia is that while companies have long been providing WH&S risk disclosure to state authorities, investment markets — including shareowners — have generally not received the same information.

Such disclosure of WH&S risk can include specialist reporting provided under the Global Reporting Initiative and disclosure in annual reports and on company websites.

The rationale behind the need for greater WH&S disclosure to investment market participants is grounded in fundamental business principles. Disclosure of WH&S provides investors with information regarding:

- WH&S as a primary financial risk
- a proxy for management competency (through time series disclosure)
- intangible asset management eg reputation and employer of choice.

As a basic requirement, companies should disclose to financial markets:

- a concise explanation of the nature of key WH&S risks facing the business
- key performance indicators used, and management programs in place to mitigate these risks
- data or information demonstrating progress as it relates to underlying business value (eg results of WH&S policies and practices on an historic basis and the objective of WH&S policies and practices on a prospective basis).

Simply, the metrics used should be appropriate to the specific risks identified by the company.

Research conducted by Monash University has confirmed that management of WH&S is not viewed as a separate function or responsibility among the more sophisticated firms in the S&P/ASX 200 Index. Rather, it is regarded as a consequence of broader initiatives targeting company productivity, competitiveness and profitability. The same research also revealed shortfalls in corporate Australia's WH&S performance. Such shortfalls represent opportunities to improve company efficiencies to the betterment of shareholder value through time.

Monash's assessment of 2001/02 disclosure practices suggests improved WH&S performance represents an opportunity for more than 50% of the S&P/ASX200 Index.

Background to Position Paper

The costs of WH&S

WH&S is an operational business cost. WH&S is both a financial cost, and a potential reputation cost. It is a cost incurred as a consequence of one or more of the following:

- → WH&S regulation and its enforcement (both national and international standards — when operating abroad)
- → the loss of corporate credibility or corporate image (reputation)
- → supply chain pressure[1]
- → a duty of care to provide a safe workplace.

WH&S is also a management function that contributes toward maximising competitive advantage through workforce loyalty, improved productivity, lowers workers compensation premiums and reputation rewards such as being an 'employer of choice'. In Australia, the direct costs of work-related injury and disease are estimated to be $27 billion per year, with indirect costs potentially up to four times greater.[2] Internationally, concern over the rising cost of WH&S has been expressed in a recent US survey that identified cost containment in the form of rising healthcare, disability and labour costs as the most critical business issue impacting employers during the coming years.[3]

Australian costs of WH&S understated

While Australian employers bear around 40% of the total direct costs of work-related injury, including costs related to workers' compensation, lost productivity and overtime,[4] many firms do not account for indirect WH&S costs. Indirect costs include the costs of management time and unproductive surveillance.[5] Nor do companies recognise the transfer of the costs outside the company. Another frequently unaccounted cost of WH&S is industrial action driven by WH&S concerns, which is now regarded as a material cause of industrial disputes in Australia.[6]

Escalating regulatory costs are likely to be incurred by Australian employers in the future. Some firms in poorly performing industries are finding it necessary to budget for the rising costs associated with the enforcement of stricter WH&S guidelines and emerging WH&S legislative obligations7. The potential for regulatory change has been underlined in 2002 with the introduction of legislation bills, in a number of Australian states, proposing criminal sanctions against directors and senior managers where serious injuries are caused by WH&S negligence. While no state has yet passed an 'industrial manslaughter' bill, this is a significant shift in the Australian business landscape.

1_Key Management Motivators in Occupational Health and Safety, KPMG Consulting (Research for the CEO and Supervisors Drivers Project commissioned by the National Health and Safety (Council) February 2001.
2_Data on OH&S in Australia — the Overall Scene, National Occupational Health and Safety Commission, Sydney, October 2000.
3_Productive Workforce Survey, Total Health Advocacy Partners, The California Public Employees' Retirement Systems and Andersen, May 2002. This was a nationwide survey in the US surveying more than 1,500 public agencies and private employers.
4_Industry Commission Inquiry into Work, Health and Safety — Volume 1, 1995.
5_Marson, G K. The 'value case' for investment in occupational health, Occupational Medicine, Vol 51 no 8 pp.496–500, Oct 2001.
6_Terence Cole, Royal Commissioner of inquiry into the building industry, quoted in Call for safety shake-up, The Age, 7 May 2002.

Current WH&S practice in Australian listed companies

WH&S risk management

Currently, fewer than one in four of Australia's largest listed companies report having a WH&S management system that demonstrates a commitment to comprehensive risk identification, assessment and control.

The identification, adequate assessment and appropriate control of risk is a part of all business management processes. A systematic management approach to determine acceptable levels of WH&S risk and measures to control that risk based on comprehensive risk assessment should be in place in all S&P/ASX200 companies.

Accountability for WH&S

Good WH&S performance depends on the action of workplace participants including executives, line supervisors and employees. Only 27% of S&P/ASX200 companies publicly identify senior managers and decision-makers responsible for WH&S. This research finding falls short of the near 40% of S&P/ASX200 companies that can be categorised as being in 'high risk' business sectors.

To demonstrate a sound system of internal controls, all companies should:

- → allocate personal accountability at senior management or executive level ('responsible officer')
- → demonstrate to investors clear and considered internal management reporting lines to respond to WH&S risks.

Reporting WH&S

Stakeholders and investors expect annual reports and supporting corporate publications to detail a company's operational risks and comprehensively state its financial and market position. Corporate reporting should therefore address WH&S performance, including measures that demonstrate:

- → a principled approach to WH&S programs (rather than a prescriptive, rules-based approach) involving workforce participation in the identification and control of WH&S risks
- → the effectiveness of WH&S management systems in identifying, assessing and controlling health and safety risks.

These reporting reforms would represent a significant improvement on current practice where an unacceptable minimum of just over one in five companies in the S&P/ASX200 report workplace injury data to investors.

WH&S risk management under greater scrutiny from institutional investors

The WH&S profile of Australian companies has received increased investor focus since the introduction of the Financial Services Reform Act (FSRA) in March 2002. The FSRA imposes new disclosure obligations on providers of investment products, including disclosure of the extent to which labour standards are taken into account in the selection, retention or realisation of an investment.[1] To date, no specific guidance has been provided on the meaning and application of labour standards; however, it would appear logical and appropriate that this should include consideration of WH&S.

Additional investor focus on WH&S has increased with the growth of socially responsible investment (SRI) funds in Australia. Since 1996, the number of dedicated SRI funds offered in the Australian market has grown from 11 to around 74 in 2002.[2] By July 2002, approximately 20 superannuation funds offered an SRI fund as a member investment choice, representing a significant portion of the total superannuation industry[3] and markedly increasing the potential for investment benefits for preferred sustainable companies. Elevated scrutiny is likely to result in calls for companies to demonstrate greater transparency so that investors can make a comprehensive assessment of their investment risk.

1_S.7.9.14C Labour standards and environmental, social and ethical considerations, Financial Services Reform Act. A similar provision exists in the UK and similar regulations are being considered in Germany, France, Canada and the European Commission.

2_Including superannuation funds, charitable funds, community finance investment, managed and private SRI funds and investments by charitable organisations (Ethical? Investment, A review of the SRI industry in Australia. Total Environment Centre 2002).

3_As of June 2002, SRI options through member choice had become available to over 2 million Australians.

The essentials in leading-edge WH&S practice

WH&S management can be seen as a microcosm of risk management generally, and is therefore of interest to all investors and other company stakeholders. A well-managed company should, as a minimum, demonstrate to institutional investors that it adheres to the following three principles:

→ comprehensive and integrated WH&S risk management
→ specific and senior accountability for WH&S (‘responsible officer’)
→ adequate WH&S reporting to allow investors to form an accurate opinion of a firm’s WH&S standing.

The safety of the workplace for employees, contractors, customers, the public — and even more broadly, the safety of its products to end users — is vital to the ongoing success of any company’s production processes and the enhancement of its long-term business value. The link between corporate WH&S performance, productivity, quality and financial performance can be seen as a key to the establishment of healthy, sustainable company’s.

WH&S management

WH&S injury risks include physical, technical, organisational, social, economic and human aspects of the workplace. As each of these aspects could be relevant to injury prevention, all should be included in a risk-based prevention strategy. For example, information on each relevant variable should be systematically collected and assessed to give a full description of the occupational and social environment of the workplace. This will ensure the effectiveness of the prevention strategy by taking into account all relevant factors in terms of the situation, workplace group and health and safety outcome.[1]

A company’s system of internal control contributes to the fulfilment of its business objectives and therefore to safeguarding shareholder value and the company assets.[2] Consequently, integrating WH&S risk management into a company’s strategic plan and everyday business processes should reflect sound business practice. Examples of such integration include:

→ systems ensuring upstream reporting to senior management with defined WH&S responsibilities
→ linking WH&S indicators with other areas of business performance (such as pay)
→ extending WH&S management to hired labour, contractors and suppliers.

For investors, the link between effective WH&S risk management and higher productivity, reduced absenteeism, lower healthcare costs and reduced worker compensation costs suggests that a company that manages its WH&S program well is also likely to be well managed financially.

In the short term, the financial benefits of reducing the direct costs of WH&S can be significant. The average cost of absenteeism, often associated with poor WH&S performance, was $US602 per-employee in the US with unscheduled absenteeism considered a serious problem by 41% of US employers.[3] Leading Australian companies have related WH&S factors for management and employee key performance indicators (KPI’s).

According to recent studies, the rewards of good WH&S management are self-reinforcing — an increase in employee trust in management leads to enhanced safety performance.[4] This ought to encourage innovation in risk management, which is important in supporting paper-based risk management mechanisms, especially through increased workforce participation and accountability with respect to WH&S. As a further example, internal health and safety committees have been linked to a ‘highly significant’ impact on injury rates,[5] leaving the door open for new and innovative ways to encourage workforce participation and management accountability for WH&S.[6]

1_Larsson, TJ and Field, B. ‘Strategic Occupational Injury Prevention: The Distribution of Occupational Injury Risks in the State of Victoria’, June 2000.
2_Internal Control: Guidance for Directors on the Combined Code, The Institute of Chartered Accountants in England & Wales together with the London Stock Exchange.
3_Unscheduled Absence Survey, 2000, CCH.
4_How to Improve Safety by Earning Employee’s Trust, Safety Director’s Report, Institute of Management & Administration, 4 January 2002) Note — evidence is considered compelling but inconclusive.
5_Journal of Occupational and Environmental Medicine, December 2001.
6_See Geller, E. S. The Participation Factor, American Society of Safety Engineers, http://www.asse.org.

Accountability for WH&S

Accountability is critical for the quick and effective control of WH&S alongside integrated risk management systems and transparency through external reporting. To discharge personal liabilities and to ensure the control of corporate credibility and image, senior management or the executive group must be informed of critical WH&S information. Likewise, the responsibility for communicating work-place hazards at an operational level is best discharged by employees and their immediate supervisors.

Clear reporting channels within each firm should specify areas of accountability and provide incentives for timely and comprehensive internal reporting. This will facilitate proactive and informed WH&S decisions by the persons responsible.

Reporting on WH&S

In most cases, although the law places companies under a duty of care to provide a safe workplace and to monitor their operations to ensure safety risks are controlled, no comprehensive legislation requires a company to disclose this information in its reporting.

A number of recent initiatives have bought the risks of WH&S closer to the financial markets. The Global Reporting Initiative,[1] backed by the United Nations, provides companies with a framework for reporting financial and non-financial information to their stakeholders. In the UK, the Health and Safety Commission published a guidance note assisting directors to compile health and safety information for annual reports.[2] A number of Australian WorkCover Authorities have also commissioned similar guidance material.[3]

To meet investor needs it is good practice for companies to report on WH&S performance because this provides relevant and material information to financial stakeholders, enabling them to make informed decisions about the companies risk management position.

Using appropriate indicators in reporting

Internal safety indicators allow a company to identify, monitor, assess and control risks in the workplace. WH&S indicators provide senior management with feed-back on indicators of performance in key areas so that WH&S performance can be continually monitored and reviewed.

For investors, best-practice management of WH&S can serve as a proxy for a responsible and effective management approach to risk identification, assessment and control. Management indicators therefore link sound WH&S management with good risk management, management systems more generally and ultimately with business health.

Indicators used in corporate publications should therefore provide investors with a picture of management health, using both positive and negative performance indicators.

Positive performance indicators are measures of proactive activity necessary to control loss or damage; and negative performance indicators focus on outputs and outcomes. These measures help investors assess the commitment of an organisation to long-term investment in WH&S management and can demonstrate innovation in risk control. Examples include decisions to invest in WH&S through comprehensive workforce training, or making resources available for WH&S programs such as management system audits.

Companies can report positive performance in terms of training investment per dollar of revenue, or in terms of hours of training received by each employee per year as nominated by the American health and safety professionals for 2002.[4]

Negative performance measures, such as the injury incidence rates, return to work figures and the cost of workplace injuries and illnesses, provide valuable historic trend data. In any event, whether using positive or negative performance indicators, data or information should demonstrate progress as it relates to underlying business value and the metrics used should be appropriate to the specific risks identified by the company.

1_See http://www.globalreporting.org.
2_Health and safety in annual reports: Guidance from the Health and Safety Commission, 2001. See also 'Director Action on Safety — Measuring and Reporting on Corporate Health and Safety Performance Towards Best Practice', Royal Society for the Prevention of Accidents, 2001 (http://www.rospa.org.uk/cms/STORE/Occupational%20Safety/4_index_files/).
3_Occupational Health and Safety Reporting: Guidelines for reporting OHS in annual reports, Victorian Workcover Safety, 2000. See also references in the Turnbull Report (Internal Control: Guidance for Directors on the Combined Code Institute of chartered Accountants in England and Wales on Corporate Governance, September 1999), and http://www.oecd.org/daf/investment/guidelines/mnetext.htm and http://www.workcover.vic.gov.au/dir090/vwa/publica.nsf/Site+Search/3AE594FCFD959D1F4A256AFF0007CB93.
4_19th Annual ISHN White Paper, Industrial Safety and Hygiene News, Devon, Pa.;610–2540–9877; http://www.ishn.com — National US survey of 221 full-time safety professional.

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