Corporate Social Responsibility from the Top Down: Meeting Board & Investor CSR Expectations

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Partner, Ropes & Gray LLP
As part of his practice, for almost 30 years, Michael has been active in advising leading public and private companies on ESG, business and human rights, corporate social responsibility and supply chain compliance matters, and he is widely viewed as the leading practitioner in this emerging area.

Michael advises clients on, among other things:

- Compliance with a wide range of enacted, pending and proposed regulatory requirements; “soft law” instruments; and industry and NGO codes of conduct, standards, frameworks and guidance.
- Due diligence.
- Risk and impact assessments.
- Structuring and implementation of tailored compliance policies, procedures, programs and codes of conduct.
- Public benefit corporations.
- Impact investing.
- Green bonds.
- Training.
- Benchmarking.
- Regulatory and voluntary disclosures and other communications.
- Stakeholder engagement.
- Grievance mechanisms.
There is no single agreed upon terminology or set of definitions
<table>
<thead>
<tr>
<th>Environmental</th>
<th>Social</th>
<th>Governance</th>
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</thead>
<tbody>
<tr>
<td>Air and water pollution</td>
<td>Customer satisfaction</td>
<td>Anti-competitive behavior</td>
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<tr>
<td>Biodiversity</td>
<td>Data protection and privacy</td>
<td>Board composition and committee structure</td>
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<td>Carbon reduction/Climate change</td>
<td>Diversity and equal opportunity</td>
<td>Bribery and corruption</td>
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<td>Deforestation</td>
<td>Employee attraction and retention</td>
<td>Business ethics</td>
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<td>Energy efficiency</td>
<td>Employee engagement</td>
<td>Compliance</td>
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<td>Hazardous materials</td>
<td>Government and community relations</td>
<td>Disclosure practices</td>
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<td>Land degradation</td>
<td>Human capital management</td>
<td>Executive remuneration</td>
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<td>Regulatory change</td>
<td>Human rights</td>
<td>Lobbying</td>
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<td>Resource depletion</td>
<td>Indigenous rights</td>
<td>Political contributions</td>
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<td>Waste management</td>
<td>Labor standards</td>
<td>Risk management</td>
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<td>Water management</td>
<td>Labor-management relations</td>
<td>Stakeholder dialogue</td>
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<td>Water scarcity</td>
<td>Marketing communications</td>
<td>Succession planning</td>
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<td>Product mis-selling</td>
<td>Whistleblower schemes</td>
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<td></td>
<td>Product safety and liability</td>
<td></td>
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<td></td>
<td>Supply chain management</td>
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<td></td>
<td>Workplace health and safety</td>
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ESG and the Board: A Confluence of Drivers

Corporate Purpose

Litigation

Shareholder Proposals

ESG Integration

Data Analytics

Disclosure

Regulation

Other ESG Drivers:

Commercial Customers

Employees

NGOs

Peers & Competitors

Mitigate Risk

Reputation & Publicity

“Do the Right Thing”

Industry Codes of Conduct
Statement on the Purpose of a Corporation

While each of our individual companies serves its own corporate purpose, we share a fundamental commitment to all of our stakeholders. We commit to:

• **Delivering value to our customers.** We will further the tradition of American companies leading the way in meeting or exceeding customer expectations.

• **Investing in our employees.** This starts with compensating them fairly and providing important benefits. It also includes supporting them through training and education that help develop new skills for a rapidly changing world. We foster diversity and inclusion, dignity and respect.

• **Dealing fairly and ethically with our suppliers.** We are dedicated to serving as good partners to the other companies, large and small, that help us meet our missions.

• **Supporting the communities in which we work.** We respect the people in our communities and protect the environment by embracing sustainable practices across our businesses.

• **Generating long-term value for shareholders,** who provide the capital that allows companies to invest, grow and innovate. We are committed to transparency and effective engagement with shareholders.

Each of our stakeholders is essential. We commit to deliver value to all of them, for the future success of our companies, our communities and our country.

Signed by approximately 200 BRT members
"[A] company’s ability to manage ESG matters demonstrates the leadership and good governance that is so essential to sustainable growth, which is why we are increasingly integrating these issues into our investment process.”

dBlackRock (2018)

"Unnerved by fundamental economic changes and the failure of government to provide lasting solutions, society is increasingly looking to companies, both public and private, to address pressing social and economic issues. These issues range from protecting the environment to retirement to gender and racial inequality, among others.”

BlackRock (2019)

“Our primary fiduciary obligation to our clients is to maximize the long-term returns of their investments. It is our view that material environmental and social (sustainability) issues can both create risk as well as generate long-term value in our portfolios. This philosophy provides the foundation for our value-based approach to Asset Stewardship.”

State Street (2019)

"Investors are moving from exclusionary screens to proactive consideration of ESG factors pre- and post-investment."
**ESG Engagement Topics**

- Board composition, effectiveness and accountability
- Strategy, purpose and culture
- Compensation that promotes long-termism
- Management of environmental risks and opportunities
- Regulatory compliance
- Supply chain management
- Human capital management
- Labor standards and human rights

“The board’s role in overseeing management’s implementation of long-term strategy and reinvestment in the business for future growth continued to be an area of focus. Woven through many of these discussions was how company leadership ensures that they have a sustainable business model. This includes how they are managing and reporting on the material environmental and social impacts of their operations. Over our clients’ long-term investment horizon, in our experience, companies with leading practices in these areas are more likely to deliver sustainable financial returns.”

*BlackRock 2019 Investment Stewardship Annual Report*

“In many situations, social issues and the views of outside stakeholders will be relevant to companies’ long-term financial success, and we expect directors to closely monitor those issues. If a company’s practices, organizational culture, or products put people’s health, safety, or dignity at risk, they can pose a financial risk to investors too.”

*Vanguard Investment Stewardship 2019 Annual Report*

**Stewardship Statistics**

**BlackRock**

2,050 engagements with 1,458 companies; 256 engagements on environmental risks and opportunities; team expanded from 36 to 45.

Twenty-seven percent of approximately 700 engagements involved E&S; voted against management on 19 percent of E&S proposals, including 75 percent of 2°C scenario proposals; in 2019, launched R-Factor, which measures the performance of business operations and governance as it relates to financially material ESG challenges, drawing on data from ESG data providers and leveraging materiality frameworks such as SASB.

**Vanguard**

868 engagements, up from 721; met with independent directors in nearly 50 percent of engagements; engaged with 258 companies in carbon-intensive industries.
Driver 3: ESG Data Analytics Continue to Proliferate
Driver 4: E&S Proposals Are Becoming a More Important Engagement Tool

E&S Proposals outnumbert governance proposals in early 2019
number of shareholder proposal filings by proposal category (2019 ytd)

<table>
<thead>
<tr>
<th>Proposal Category</th>
<th>2017</th>
<th>2018</th>
<th>2019</th>
</tr>
</thead>
<tbody>
<tr>
<td>Human Rights</td>
<td>38</td>
<td>36</td>
<td>31</td>
</tr>
<tr>
<td>Human Capital</td>
<td>31</td>
<td>35</td>
<td>21</td>
</tr>
<tr>
<td>Social - Other</td>
<td>17</td>
<td>18</td>
<td>14</td>
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<tr>
<td>Climate Change</td>
<td>59</td>
<td>54</td>
<td>38</td>
</tr>
<tr>
<td>Environmental</td>
<td>21</td>
<td>45</td>
<td>34</td>
</tr>
<tr>
<td>Governance/Compensation</td>
<td>104</td>
<td>60</td>
<td>14</td>
</tr>
<tr>
<td>Total</td>
<td>439</td>
<td>332</td>
<td>329</td>
</tr>
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Source: Georgeson

11 E&S Proposals Received
Majority Support in 2019

- Board diversity (2)
- Executive diversity
- Workplace diversity
- Opioid risk report (2)
- Human rights report
- Lobbying disclosure
- Political spending disclosure (3)
# Driver 5: Legal Requirements & Soft Law Instruments Continue to Be Adopted

<table>
<thead>
<tr>
<th>Adopted</th>
<th>Pending/Proposed</th>
<th>Voluntary</th>
</tr>
</thead>
<tbody>
<tr>
<td>California Transparency in Supply Chains Act</td>
<td>U.S. Business Supply Chain Transparency on Trafficking and Slavery Act</td>
<td>UN Guiding Principles on Business and Human Rights</td>
</tr>
<tr>
<td>U.S. Federal Acquisition Regulation Anti-Human Trafficking Provisions</td>
<td>Netherlands Child Labour Due Diligence Law</td>
<td>OECD Guidelines for Multinational Enterprises</td>
</tr>
<tr>
<td>UK Modern Slavery Act</td>
<td>Canadian Modern Slavery Act</td>
<td>OECD Due Diligence Guidance for Responsible Business Conduct</td>
</tr>
<tr>
<td>U.S. Trade Facilitation and Trade Enforcement Act</td>
<td>Canadian Transparency in Supply Chains Act</td>
<td>OECD Sector Guidance</td>
</tr>
<tr>
<td>Countering America’s Adversaries Through Sanctions Act</td>
<td>New South Wales Modern Slavery Act</td>
<td>International Labour Organization Labor Standards</td>
</tr>
<tr>
<td>French Corporate Duty of Vigilance Law</td>
<td>Hong Kong Modern Slavery Legislation</td>
<td>UN Sustainable Development Goals</td>
</tr>
<tr>
<td>U.S. Conflict Minerals Rule</td>
<td>Swiss Responsible Business Initiative/Council Counter-Proposal</td>
<td>Sustainability Accounting Standards Board, Global Reporting Initiative, CDP and the United Nations Global Compact</td>
</tr>
<tr>
<td>California Director Diversity Legislation</td>
<td>UN Treaty on Business and Human Rights</td>
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<tr>
<td>Australian Commonwealth Modern Slavery Act</td>
<td>German Human Rights/Supply Chain Legislation</td>
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</table>

**Red:** Adopted or implemented since January 1, 2017

**Green:** Proposed since January 1, 2018
Driver 6: Disclosure Is Increasing & Becoming More Investor-Focused

Common Considerations:
- Materiality and priorities
- Audience
- Level of disclosure
- Placement
- Frameworks
- Targets
- External assurance

“In considering the options available, we have identified the Sustainability Accounting Standards Board (SASB) and the Financial Stability Board’s (FSB) Task Force on Climate-related Financial Disclosures (TCFD) as the most useful reporting frameworks for issuers and investors alike, and we have been actively involved in efforts to broaden acceptance of these frameworks.”

*BlackRock 2019 Investment Stewardship Annual Report*

“We have consistently advocated for company disclosure that aligns with industry-established reporting frameworks such as the Task Force on Climate-related Financial Disclosures, and we have seen increased reporting that is both comparable and decision-useful for investors.

“Because required disclosures don’t tell the whole story, we encourage companies to use disclosure frameworks to guide their presentation of information in a way that is consistent, comparable, and relevant to investors.”

*Vanguard Investment Stewardship 2019 Annual Report*
Driver 7: CSR Litigation & Enforcement Is Increasing

- UK Home Office MSA statement compliance sweep.
- California city attorney claims.
- National Contact Point Specific Instance proceedings.
- Modern slavery disclosure lawsuits (California, MA and France).
- Anti-Terrorism Act lawsuits against pharmaceutical and medical device companies.
- California and New York climate change litigation.
- Lafarge French judicial inquiry (Syria).
- FIFA lawsuit (Qatar).
- Bangladesh Accord arbitrations.
- CAATSA requests.
- TVPA lawsuits.
- OFAC supply chain enforcement.

Shareholder Litigation: The Next Big Thing?
The Role of the Board & Senior Management in ESG

• Embed within senior management and board oversight structures.
  – At committee and full board level.
  – Consider whether to incorporate into board charters.
  – Starting in 2019, Glass Lewis identifies S&P 500 Index directors who have been assigned specific oversight of E&S issues at the committee level.
• Include as part of strategic planning and risk oversight.
  – Set clear priorities, goals and targets that are connected to corporate performance and risk.
  – Drive materiality/priority assessments.
• Obtain regular updates.
• Build director skills around E&S.
• Know what investors care about.
• Ensure appropriate allocation of resources.
• Set “tone from the top.”
  – Statements, policies, procedures, training and incentives.

“In our experience, most governance issues, including how relevant environmental and social factors are managed, require board leadership and oversight.”

BlackRock 2019 Engagement Priorities

“Every company needs a framework to navigate this difficult landscape [‘the global landscape is increasingly fragile and, as a result, susceptible to short-term behavior by corporations and governments alike’], and that it must begin with a clear embodiment of your company’s purpose in your business model and corporate strategy. Purpose is … a company’s fundamental reason for being – what it does every day to create value for its stakeholders. [W]hen a company truly understands and expresses its purpose, it functions with the focus and strategic discipline that drive long-term profitability. Purpose … drives ethical behavior and creates an essential check on actions that go against the best interests of stakeholders. Purpose guides culture, provides a framework for consistent decision-making, and, ultimately, helps sustain long-term financial returns for the shareholders of your company.”

Larry Fink’s 2019 Letter to CEOs
For additional compliance resources, visit:
Q&A
QUESTIONS?
slido | #Insight19