

# Corporate Social Responsibility and Sustainability in Troubled Times: Implications for Directors

This is the time for corporate social responsibility (CSR) and sustainability. There are three reasons that directors need to ensure attention to CSR and sustainability within their organisations:

- CSR and sustainability have become key elements of an organisation's demonstration of its alignment with the values of the societies in which it does business. The current crisis will place greater pressure on organisations to demonstrate that alignment.
- Regulation is going to increase in both span and intrusion. There exists the perception that deregulation or self-regulation has contributed to the current crisis. This will lead to greater direct oversight and regulation of businesses. Organisations own statements of commitment to CSR and sustainability will be backed up by regulation.
- Directors need confidence that the CSR and sustainability information that is externally reported is accurate, and will not result in public relations, regulatory or negative efficiency exposures to the business.

Directors should be taking the time now to ensure that CSR and sustainability are appropriately prioritized, to establish their credentials in the market, and to ensure that they are prepared for a world of greater regulated CSR and sustainability reporting.

## Background

CSR and sustainability have taken on a greater importance over the past decade, driven by a combination of regulation, operational efficiency, competitors positioning and a greater emphasis on being able to demonstrate ethical business practices. Today over 85% of the S&P100 provide some form of sustainability reporting, while virtually all of the FTSE100 provide various CSR and sustainability reports.

One thing is clear; as government and business work through the current financial crisis, we will see significant increases in regulation and increased scrutiny over financial and material non-financial information such as business strategy, governance structures, CO<sub>2</sub> emissions and social impacts. This will include the processes for creation of reported information; for both public and private organisations. Directors should expect increased emphasis on systems of internal control, and reporting obligations comparable to those we have seen introduced in the SEC registrant companies in the US (with reporting being a high probability).

CSR and sustainability demonstrate practically an organisation's standards of ethical behaviour. Increasingly, external audiences expect that strong ethical behaviour, and responsible and sustainable business and commercial practices, reflect a respect for the societies in which the organisation functions — its license to operate.

Of course, there remain those who think CSR and sustainability are not core to the business, or have treated them primarily as marketing and positioning activity. Finally, there remain some who simply discount the need and value of CSR and sustainability.

**If the organisation's CSR and sustainability reporting and processes are best practice today, are you confident that they are ready for tomorrow?**

**What are the implications on governance, performance, compliance and quality?**



### Some expectations from the crisis

Financial crises have a habit of leading directly to increased regulation. In the current environment, it is clear that the existing regulatory environment will undergo significant change. So what kind of change can we expect, and how will this impact CSR and sustainability programmes and in particular, directors' responsibilities?

Certainly, we will see significant increases in transparency requirements. As the funding gaps of companies' pension schemes become more acute, and as these funds, in greater numbers, fail to deliver against their obligations, we will see greater regulatory oversight and transparency demands across public and privately held organisations. If compensation is not directly regulated at the senior levels, we should at minimum expect to see increased compensation disclosure regulations.

We may even see compliance with the UK Combined Code move from being voluntary "with explanation", to being mandatory. We will see far greater scrutiny from regulators (we may even see whole new regulatory bodies established) of company's disclosures under the "comply or explain" principles, and should expect "or explain" clause to disappear over the coming years.

We can conclude that CSR and sustainability reporting is not going away, and will increase in importance. In fact, the UK Labour government has recently confirmed that it intends to push ahead with its aggressive greenhouse gas (GHG) reductions targets of 80% reductions through 2050.

Directors should expect to see greater emphasis on their oversight over issues relating to CSR and sustainability. Today many companies already provide a range of regulator-required reports, covering the range of environmental, health and safety, employment of other law. CSR and sustainability reporting will need to bring these disciplines together to provide consolidated

reporting along with financial information currently provided. This will include a greater emphasis on historical performance, trends and stated future targets.

### CSR and sustainability: the drivers

CSR and sustainability can be viewed as the practical expression of an organisation's ethics. It is also a proactive tool to manage and shape stakeholder expectations. Finally of course it can, and should, be viewed as a strong driver of improved business performance, providing opportunities to implement performance efficiency and effectiveness improvements across the organisation.

Balanced scorecards and strategy maps have grown into almost ubiquitous use due to their ability to help organisations consider a number of business drivers to achieve strategy. CSR and sustainability provide an additional set of measures that can positively impact overall organisational performance and that should be included in the balanced scorecard. For example, the DVFA (the German Institute of Investment Analysts) have developed a set of CSR and sustainability indicators that their members are encouraged to use in valuing companies. Organisations should consider including some of these metrics in their internal reporting.

One area of significant importance is the measurement and reporting of CO<sub>2</sub> emissions. While not covering all organisations (yet) there are two drivers that are increasing the range of organisations that must track CO<sub>2</sub> emissions. These drivers are:

- **Caps on total CO<sub>2</sub> produced.** There are organisations in carbon-intensive industries that are subject to emissions caps. These organisations must measure, report, and potentially purchase carbon credits to cover excess tons of CO<sub>2</sub> produced. Conversely, they are able to sell excess credits representing tons of CO<sub>2</sub> not produced.



- **The Carbon Disclosure Project** (a global NGO launched in 2000 at No 10 Downing Street) which is engaged in a 'name and shame' campaign to encourage organisations to report on the levels of CO<sub>2</sub> that they produce and plans on how they will reduce their CO<sub>2</sub> emissions.. To date, over 3000 organisations have provided reports to the CDP. Has yours?

As another example, historically, electricity bulk purchasing has been a procurement issue. Many organisations now pass budget responsibility for electricity consumption directly to data-centre director, with the result that a formerly hidden cost (to the data-centre director) becomes a cost element that is within his or her direct ability to manage. When viewed through the CSR and sustainability lenses, this leads to both a reduction in power consumption and therefore a corresponding reduction in tons of CO<sub>2</sub> produced, and leads to reductions in costs of data-centre overheads.

Many organisations fail to effectively link external CSR and sustainability activity to key business strategies and objectives, or to the organisations' key performance indicators. In these cases the organisation can be squandering resources pursuing non-core or non-core supporting, but socially beneficial activities.

### What can go wrong

One difficulty facing directors and organisations when considering CSR and sustainability reporting is the plethora of competing reporting standards organisations, NGOs and quasi-government organisations, each advocating for compliance with their frameworks, standards or formats for content of reporting. This places pressure on organisations to determine which standards or formats they will use.

For example, Directors should have confidence that any CO<sub>2</sub> reduction targets and actual results reported in

### Key findings

from Ethical Investment Research Services, July 2008

#### Many large cap companies at risk

Over a third (35.6%) of companies in the global 300 are high or very high impact for climate change (representing over USD 6.8 trillion market cap)

#### High risk companies have taken initial steps but translation into coherent strategy is less apparent

84% of high-risk companies have a corporate-wide climate change commitment. But only 14% link board remuneration to climate change strategies. **Only 25% publish a long-term strategic target to reduce emissions**

#### Emissions disclosure by high risk companies is high but unreliable

**81% disclose either absolute or normalised data but only 9% disclose the scope of their emissions against the GHG**

sustainability reports, such as a GRI (Global Reporting Initiative) compliant report, are the same data that are provided in a Carbon Disclosure Project response.

The issue for many organisations is that GRI-type CSR and sustainability reports are produced by or through the marketing function, while Carbon Disclosure Project reports are produced through the operations arm of the organisation. Too frequently the information provided in different reports has been sourced from different parts of the organisation and is inconsistent when presented to external audiences.

In almost all cases, in addition to the risk of 'multiple messages', these are the same risks that exist in reporting of financial data: accuracy, reliability, completeness, timeliness of information being reported.



Major issues for directors include simply knowing:

- What is being reported,
  - To whom,
  - Who is requesting the information,
  - Who is providing the information, and
  - The level of assurance that has been gained over the information being provided.
- What economic measures / targets exist for CSR and sustainability?
  - What governance exists providing oversight and monitoring?
  - What assurance do you need, what is provided over CSR and sustainability reports and who provides that assurance?

Finally, directors must have the confidence that the messages that are being given to the wider market are reflected in the actions of the organisation – ‘walking the talk’. This includes having confidence that the results that are being reported can be trusted, and that they represent information sourced from common and trusted systems or processes.

### Some questions for directors

How do you expect to retain the focus on CSR and sustainability in an economic downturn, or, if CSR and sustainability mattered when "things were good", does it still matter?

- What is your organisation’s CSR and sustainability strategy?
- Who is operationally responsible for CSR and sustainability?

### Actions

**If any director is not comfortable with their own answers to the questions above, there are some action steps that should be considered. These should include:**

1. Confirm the linkage between the programme and the organisation’s short and long-term strategy.
2. Request an update to the Board of Directors on the programme, the strategy, key performance indicators and key objectives of the programme.
3. Review the governance structures around the CSR and sustainability programme.
4. Confirm what assurance is being provided over report content and process.
5. Confirm how CSR and sustainability are being embedded in the organisation.

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### About the Author — Daniel Roberts

Daniel has over 25 years experience in sustainability, innovation, risk management, corporate governance, audit and information technology. Daniel established Risk & Audit Advisory Services Ltd (RAAS) in 1995, and became Grant Thornton’s US National Director of Assurance Innovation in February 2001. For the past three years he has been working in the areas of XBRL and sustainability, including developing a methodology for the implementation of CSR and sustainability programmes.