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# Corporate Social Responsibility, Corporate Sustainability, and the Role of the Board

In her regular column on corporate governance issues, Holly Gregory discusses the role of the board of directors regarding corporate social responsibility and corporate sustainability issues, including oversight, disclosure, and shareholder engagement.

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Holly counsels clients on a full range of governance issues, including fiduciary duties, risk oversight, conflicts of interest, board and committee structure, board leadership structures, special committee investigations, board audits and self-evaluations, shareholder initiatives, proxy contests, relationships with shareholders and proxy advisors, compliance with legislative, regulatory, and listing rule requirements, and governance best practice.

As investor interest in corporate social responsibility (CSR) increases, US public companies are under pressure to provide more disclosure about how they act as responsible corporate citizens while positioning themselves to succeed over the long term. To meet these pressures, boards and their advisors need to pay more attention to how consideration of CSR and corporate sustainability issues is integrated into business decision-making (including analyzing operational and strategic risks and opportunities), corporate disclosure, and shareholder engagement efforts.

**CSR AND CORPORATE SUSTAINABILITY DEFINED**

The World Business Council for Sustainable Development (WBCSD), a CEO-led organization of companies focused on sustainability, defines CSR as “the continuing commitment by business to behave ethically and contribute to economic development while improving the quality of life of the workforce

and their families as well as of the local community and society at large” (WBCSD, *Corporate Social Responsibility: Meeting Changing Expectations*, at 3, available at [wbcscd.org](http://wbcscd.org)). This definition focuses on the delivery of financial, environmental, and social benefits to a broad range of constituents, and implies voluntary action beyond the strict requirements of law.

Acting as a responsible corporate citizen helps to create broad social acceptance of corporate activity that supports sustainable economic development at the macro level. It is also closely related to corporate sustainability at the company level, which can be defined as a business approach focused on the creation of long-term shareholder value by pursuing opportunities and managing risks that derive from economic, environmental, and social developments in a manner that positions the company to thrive and exhibit resiliency. Corporate sustainability is focused on ensuring the company’s continuity and survival through addressing CSR issues such as climate change, resource scarcity, demographic shifts, and regulatory and political change. (See RobecoSAM, *Corporate Sustainability*, available at [sustainability-indices.com](http://sustainability-indices.com).)

The terms “CSR” and “corporate sustainability” are often used interchangeably, although the concept of corporate sustainability includes a focus on resiliency and survival of the corporate entity.

## INVESTOR INTEREST

According to the Conference Board, Inc., an independent business membership and research association that focuses on business issues and the public interest, corporate investment in CSR enhances market and accounting performance, lowers the cost of capital, improves business reputation, and fosters new revenue growth when channeled to product innovation (Matteo Tonello, The Conference Board, Inc., *Corporate Investment in ESG Practices* (Aug. 5, 2015), available at [corpgov.law.harvard.edu](http://corpgov.law.harvard.edu)).

Therefore, it is not surprising that investors are increasingly focused on the link between CSR, corporate sustainability, and bottom-line financial performance. As the Chairman and CEO of BlackRock, Inc., the world’s largest asset manager and a major shareholder in many companies, has written, “[o]ver the long-term, environmental, social and governance (ESG) issues — ranging from climate change to diversity to board effectiveness — have real and quantifiable financial impacts” (Annual Letter from Larry Fink, Chairman and CEO, BlackRock, to CEOs (Feb. 1, 2016), available at [blackrock.com](http://blackrock.com)).

Investors report that they view CSR issues as interconnected with corporate values and financial performance, and consider them when making voting and investment decisions. In a 2014 survey, 90% of investor respondents indicated that CSR issues “played a pivotal role” in their investment decisions (EY, *Tomorrow’s Investment Rules: Global Survey of Institutional Investors on Non-Financial Performance*, at 5 (2014)).

While CSR concerns have long been of interest to socially conscious shareholders, customers, and employees, concerted efforts by certain key public pension funds and other

institutional investors, like BlackRock, are bringing issues of environmental protection, human rights, diversity, health and safety, and corporate sustainability generally into sharper focus in boardrooms. Several large institutional investors have written letters to portfolio companies highlighting their interest in these types of issues.

For example, in January 2017, the President and CEO of State Street Global Advisors (SSGA) sent a letter to the directors of SSGA’s portfolio companies emphasizing that whether the companies “clearly [communicate] their approach to sustainability and its influence on strategy” impacts how SSGA classifies them, and that CSR issues “[o]ver the long term . . . can have a material impact on a company’s ability to generate returns” (Letter from Ronald P. O’Hanley, President and CEO, SSGA, to Board Members, at 1-2 (Jan. 26, 2017), available at [ssga.com](http://ssga.com)).



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That same month, the Chairman and CEO of BlackRock wrote to CEOs that BlackRock expects companies in which it invests to consider the factors that it believes contribute to long-term growth, including sustainability of operations, attention to environmental factors that affect the business, and recognition of the company’s role as a member of the community (Annual Letter from Larry Fink, Chairman and CEO, BlackRock, to CEOs (Jan. 24, 2017), available at [blackrock.com](http://blackrock.com)).

## BOARD OVERSIGHT

While a company’s approach to specific CSR issues is largely for management to address, the board plays a critical oversight role in CSR and corporate sustainability matters. The board is often better positioned to step back and consider a longer-term view about how these issues can impact the company. The board should encourage regular consideration of how CSR and corporate sustainability concerns are related to the company’s core values, strategic development, and risk oversight.

The board's expectations regarding the company's approach to CSR should be clearly defined and communicated throughout the company by the board and senior management. The elements of the company's CSR program will depend on its industry, the regulatory requirements applicable to the company, and the most significant CSR-related risks associated with the company's strategy and operations.

While significant elements of CSR and corporate sustainability need to reside with the full board, in particular those related to oversight of business development and strategy, the company should consider the appropriate process and locus for oversight of other CSR and corporate sustainability matters. Some large US public companies have established board committees devoted to CSR oversight.

According to a recent study, the *2016 Spencer Stuart Board Index* (available at [spencerstuart.com](http://spencerstuart.com)), 10% of S&P 500 boards disclosed that they have a separately designated public policy/CSR committee and 7% disclosed that they have a separate environmental, health, and safety committee. In addition to establishing a separate committee, the board should consider whether aspects of CSR and corporate sustainability that require more detailed and regular focus should be delegated to other committees, such as a risk-focused committee or a committee with specific relevant expertise (for example, a committee focused on technology, safety, governance, or human resources).



Search [Nominating and Corporate Governance Committee Charter](#) for a model committee charter addressing CSR efforts, with explanatory notes and drafting tips.

In addition, the compensation committee should regularly review the company's incentive compensation program to ensure that it supports, and does not undermine, the CSR program's goals. The compensation committee should also consider whether it is appropriate to link performance goals or targets to a CSR or corporate sustainability goal, such as improving energy efficiency, reducing greenhouse gas emissions, meeting health and safety targets, or improving leadership diversity (see Glass Lewis, *In-Depth: Linking Compensation to Sustainability* (Mar. 2016), available at [glasslewis.com](http://glasslewis.com)).

As with other risks that the board is responsible for overseeing, the board needs to ensure that it has the right knowledge, expertise, and skill set with respect to CSR and corporate sustainability. Some boards have recruited directors with experience overseeing CSR initiatives, such as CEOs of companies with a focus on social responsibility. Others are including these issues on the agenda of their board education efforts.

BlackRock has stated in its engagement priorities for 2017–2018 that “[f]or directors of companies in sectors that are significantly exposed to climate risk, BlackRock expects the whole board to have demonstrable fluency in how climate risk affects the business and management’s approach to adapting and

mitigating the risk” (BlackRock, *Investment Stewardship: Our Engagement Priorities for 2017-2018*, available at [blackrock.com](http://blackrock.com)).

In addition to establishing the structure for providing CSR and corporate sustainability oversight, the board needs to determine how to fit these issues into its already-packed agenda. The board should consider:

- How to include CSR and corporate sustainability concerns in the board's discussions on strategy and risk oversight.
- To what extent to include CSR and corporate sustainability topics as standalone agenda items.
- What information should be provided to directors (for example, data on how the company's efforts compare to those of its peer companies, leading industry standards, and the CSR-related priorities of key shareholders and proxy advisory firms).
- Which metrics to focus on in considering progress against CSR and corporate sustainability goals (such as those involving water usage, emissions reduction, on-the-job injuries, employee turnover, or diversity retention).
- What process to use for drafting and reviewing public disclosure about CSR and corporate sustainability efforts. While at many companies these efforts may be the responsibility of corporate communications professionals, the board should consider relying on the process that management has in place for internal review of Securities and Exchange Commission (SEC) disclosure, including use of the company's disclosure committee.

Board and appropriate committee leaders need to work with management to ensure that CSR and corporate sustainability issues are given appropriate time and attention. This will help the company avoid the potential consequences of failing to identify and mitigate related risks, which may include:

- Environmental harm.
- Damage to the company's reputation and brand.
- Unstable supply chains.
- Employee dissatisfaction or work stoppages.
- Consumer boycotts.
- Product recalls.
- Management and board distraction.
- Divestment by certain investors.
- Increased attention from activist investors.

## DISCLOSURE

Shareholders, customers, employees, and business partners increasingly expect more meaningful disclosure regarding CSR matters, and are looking beyond the financial information and risk disclosure that is required to be disclosed in SEC filings. CSR-related shareholder proposals frequently call for greater transparency about corporate policies and actions regarding a particular issue, such as political and lobbying activity, sustainability reporting, gender pay gap reporting, and child labor issues. The board and management should

## SEC Disclosure Requirements Relevant to CSR

The following SEC disclosure requirements most commonly trigger disclosure of CSR matters:

<b>Regulation S-K Item 101</b>	Business description disclosure
<b>Regulation S-K Item 103</b>	Legal proceedings disclosure
<b>Regulation S-K Item 303</b>	MD&A disclosure of material known events and uncertainties
<b>Regulation S-K Item 503(c)</b>	Risk factor disclosure
<b>SEC Release Nos. 33-9106; 34-61469; FR-82 (Feb. 8, 2010)</b>	Guidance regarding climate change disclosure
<b>Exchange Act Rule 13p-1</b>	Conflict minerals disclosure

balance transparency with concerns about protecting strategic information and the time commitment and costs associated with enhanced disclosure.

The majority of large US public companies engage in some type of disclosure of CSR initiatives. The Governance & Accountability Institute, Inc. recently reported that 81% of S&P 500 companies published a corporate responsibility/sustainability report in 2015 (Governance & Accountability Institute, Inc., *Flash Report: Eighty One Percent (81%) of the S&P 500 Index Companies Published Corporate Sustainability Reports in 2015* (2016), available at [ga-institute.com](http://ga-institute.com)). However, the Sustainability Accounting Standards Board (SASB) found that while 81% of over 700 companies surveyed disclosed CSR-related risks, 52% of them used boilerplate language and did not disclose plans to address the risks (SASB, *The State of Disclosure Report 2016*, available at [sasb.org](http://sasb.org)).

The board and management should determine the preferred content of CSR disclosure and the related advantages and disadvantages. They might choose to:

- Provide only required disclosure.
- Discuss matters that investors specifically raised.
- Voluntarily disclose additional information, such as how the company's long-term strategy incorporates corporate sustainability considerations.

The board should be involved in the decision about whether to publicly disclose CSR goals, including which metrics to use and how frequently to report on progress toward those goals. In addition, the board should consider the potential for heightened litigation risk as a result of enhanced CSR disclosure. Companies should consider whether additional disclosure is appropriate, such as discussing goals or performance targets tied to CSR matters that may trigger compensation payouts.

Investors are pressuring the SEC to mandate additional CSR disclosure. Of the more than 275 non-form comment letters that were submitted in response to the SEC's April 2016 concept release on disclosure required by Regulation S-K, two-thirds specifically addressed CSR disclosure. Of these, 80% called for enhanced disclosure about CSR issues in SEC filings (SASB, *Business and Financial Disclosure Required by*

*Regulation S-K — the SEC's Concept Release and Its Implications*, at 3-4 (2016), available at [sasb.org](http://sasb.org)). While it is unlikely that the SEC will prioritize the expansion and strengthening of CSR-related disclosure requirements under the current administration, investors are likely to continue to push for greater disclosure and advocate for enhanced comparability of the CSR and corporate sustainability information that is disclosed.

Many companies are subject to additional CSR disclosure requirements under state or international laws. For example, certain companies doing business in California must disclose measures they take to eliminate slavery and human trafficking in their supply chains.



Search [Corporate Social Responsibility and the Supply Chain](#) for more on relevant CSR legislation, including the California Transparency in Supply Chains Act of 2010 and the SEC's conflict minerals rule.

In addition to required disclosure, public companies should consider other benchmarks when deciding whether and what to disclose regarding CSR. The most well-known benchmarks are the:

- Global Reporting Initiative (GRI) Sustainability Reporting Standards, which GRI considers to represent the global best practice for reporting on various economic, environmental, and social impacts (last updated in October 2016, available at [globalreporting.org](http://globalreporting.org)).
- SASB Implementation Guide for companies seeking to implement sustainability accounting standards within their existing business functions and processes (released in January 2016, available at [sasb.org](http://sasb.org)).

Companies should also consider, on an ongoing basis, what their peers are disclosing about CSR and corporate sustainability issues.



Search [Corporate Sustainability and Disclosure](#) for more on corporate sustainability disclosure, including identification of mandatory requirements for, and selected voluntary guidelines on, corporate sustainability disclosure.

The board and management should be aware that making CSR disclosure in SEC filings might carry a greater risk of liability compared to making disclosure in a separate corporate sustainability report or on the company's website, and should determine the preferred placement of the disclosure accordingly. Several companies now include CSR disclosure in the proxy statement, in line with a broader trend towards using proxy statements as a tool to communicate with investors, and not just as a compliance document. Companies are also increasingly linking to sustainability reports in their SEC filings. As part of its risk oversight and compliance duties, the board (or the relevant committee) should ensure that a comprehensive internal reporting process is in place for CSR and corporate sustainability disclosure.

### SHAREHOLDER ENGAGEMENT

Given shareholders' heightened focus on CSR issues, the board should determine which members of the board and management will engage with shareholders on CSR matters and the specific CSR matters they will focus on during engagement. Factors that might influence these determinations include the identity of the shareholder and the materiality of the subject. For example, it might be appropriate for the CEO and chairman of the board to participate in engagement involving the company's largest shareholders or issues that could significantly impact the company's operations or reputation. Directors who engage with shareholders on CSR issues should be knowledgeable about how those issues impact the company and how related risks are managed.

Companies can use several methods to assess the priorities of their shareholders with respect to CSR issues. In addition to reviewing shareholders' specific requests for CSR disclosure, the SASB Implementation Guide can aid companies in identifying industry-specific CSR topics that are likely to be material to their shareholders.

The board and management can also review their top institutional investors' CSR-related investment decisions and policies. For example, SSGA recently outlined its expectations

on how the board can work with management to incorporate sustainability into long-term strategy (SSGA, *Incorporating Sustainability Into Long-Term Strategy* (Jan. 23, 2017), available at [ssga.com](http://ssga.com)).


SSGA's framework for evaluating companies' sustainability efforts identifies issues that the board should consider, including whether:

- The company has identified the sustainability issues material to the business.
- The company has analyzed and incorporated sustainability issues, where relevant, into its long-term strategy.
- The company considers long-term sustainability trends in capital allocation decisions.
- The board is equipped to adequately evaluate and oversee the sustainability aspects of the company's long-term strategy.
- The company's reporting clearly articulates the influence of sustainability issues on strategy.
- The board incorporates key sustainability drivers into performance evaluation and compensation programs.

Shareholder proposals are also a key source of information for companies about investor priorities and support for CSR issues. The number of CSR-related shareholder proposals has increased significantly in recent years, and levels of shareholder support for these proposals continue to rise.

According to the Institutional Shareholder Services Inc. (ISS) Governance Analytics Database, 193 CSR-related shareholder proposals have been voted on at 2017 annual meetings as of June 11, 2017 (where voting results are available). Six of these proposals passed (three relating to climate change policies, two relating to board diversity, and one relating to sustainability reporting). The most prevalent issues addressed in the CSR-related shareholder proposals that have been voted on at 2017 annual meetings as of June 11, 2017 (where voting results are available) are:

- Lobbying disclosure (36 proposals).
- Climate change reporting (21 proposals).
- Political contributions disclosure (17 proposals).



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- Gender pay gap disclosure (12 proposals).
- Sustainability reporting (ten proposals).

An additional 28 CSR-related shareholder proposals are scheduled to go to a vote or have been voted on (with results pending) at 2017 annual meetings, according to ISS data as of June 11, 2017.

By comparison, in 2016, shareholders voted on 240 CSR-related shareholder proposals (out of 433 submitted), and nine received majority support (a record high). These nine CSR-related shareholder proposals focused on:

- Board diversity.
- Political contributions disclosure.
- Methane emissions management.
- Sustainability reporting.
- Animal welfare.
- Prohibition of sexual orientation and gender identity discrimination.
- Gender pay gap disclosure.

Average support for CSR-related proposals reached 20.5% in 2016, up from 20.1% in 2015, but down from 21.9% in 2014 (ISS, *United States 2016: Proxy Season Review – Environmental and Social Issues* (Oct. 26, 2016), available at [isscorporatesolutions.com](http://isscorporatesolutions.com) (subscription required)). The trend toward increasing numbers of, and support for, CSR-related shareholder proposals is expected to continue in 2017, particularly in relation to climate risk.

Ceres, a non-profit sustainability advocacy organization, conducts an annual review of the proxy voting records of major mutual funds and investment firms on CSR-related shareholder proposals. According to Ceres, SSGA supported 46% of shareholder proposals relating to climate change in 2016. However, BlackRock and Vanguard did not support any climate-related shareholder proposals. (Rob Berridge, Ceres, *Is Your Mutual Fund Company Taking Climate Change Seriously?* (Jan. 6, 2017), available at [ceres.org](http://ceres.org).) Some asset managers are now on the receiving end of CSR-related shareholder proposals for their own 2017 annual shareholders' meetings, indicating the increasing pressure on institutional investors that vote against or abstain from voting on CSR-related shareholder proposals.

CSR-related shareholder proposals commonly seek enhanced disclosure of the company's policies and actions regarding a particular CSR issue. Through shareholder engagement, companies often can negotiate the withdrawal of shareholder proposals by committing to provide additional CSR disclosure, such as a report on sustainability, political contributions and lobbying, or the gender pay gap.

## LOOKING AHEAD

As investor focus on CSR and corporate sustainability intensifies, board attention to the link between CSR and financial performance over the long term will intensify as well, with an emphasis on how economic, environmental, and social trends impact corporate strategy and risk oversight, and how these issues relate to corporate values. Heightened interest in how



# Heightened interest in how boards and management teams integrate consideration of sustainable business practices into operational decision-making, risk management, and incentive compensation programs will drive pressures for additional disclosure.

boards and management teams integrate consideration of sustainable business practices into operational decision-making, risk management, and incentive compensation programs will drive pressures for additional disclosure.

As CSR disclosure trends and shareholder priorities evolve, boards and corporate managers will need to stay abreast of developments. Often, providing enhanced disclosure may benefit the company by getting its story out to the broadening audience that cares about these issues. However, in all instances, boards and corporate managers must be cognizant of the need to protect sensitive strategic information, manage litigation risk, and consider the time and cost of enhanced disclosure.

*The views stated above are solely attributable to Ms. Gregory and do not necessarily reflect the views of Sidley Austin LLP or its clients.*