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On the board's agenda | US

The board's role in corporate social purpose

Why social purpose?

In a 1970 *New York Times* article, Milton Friedman proclaimed that the business of business was business, and corporations primarily need to focus on shareholder value. The corporate perspective has evolved significantly since then, though there is ongoing debate as to whether a commitment to social purpose activities detracts from profitability and growth.

The current state of play is reflected in a number of statements and policies issued in 2017 and 2018 by major institutional investors that both reinforce Friedman's point—the business of business is business—and simultaneously reject the notion that social purpose must come at the expense of sustaining and growing a for-profit operation.

These statements and policies build on a series of significant trends related to corporate social purpose in recent years: the growing significance of corporate social impact activities, as 90% of public companies now practice some form of social purpose,[1] the repositioning of social purpose as a viable strategy for building competitive advantage, and a virtual explosion of investor interest—including significant interest by "mainstream" investors—beginning in 2016, and continuing into the 2018 annual meeting season.

This *On the Board's Agenda* explores how social purpose strategies, programs, and investments can be important assets, and how boards might enhance their oversight of their companies' social purpose roles and actions.

1. https://www2.deloitte.com/us/en/pages/operations/articles/driving-corporate-growth-through-social-impact.html

What is corporate social purpose?

Corporate social purpose is broader than traditional corporate social responsibility (CSR) activities and encompasses how the core business delivers positive economic, social, and environmental impact in the world. Historically companies have conducted philanthropic activities through CSR units, including sponsorships, employee matching and volunteerism, and corporate foundation grants. More recently, many companies are fulfilling their social purpose in ways that cut across the entirety of the business, such as:

- paying attention to the human rights and environmental performance of the supply chain and vendors;
- respecting and supporting diversity in areas such as hiring, training, and pay equity;
- treating employees properly, including by providing a safe, harassment-free, and supportive workplace;
- safeguarding the environment through strong compliance and sound practices, both generally and in the communities in which the company operates;
- supporting their communities through such things as educational, recreational and cultural activities, advocacy of human rights, and fair labor practices;
- pursuing shared value initiatives that address social issues through core business and inclusive market solutions; and
- demonstrating board oversight of the company's role in political spending and government affairs.

A corporate social purpose perspective expands the definition of a corporation's stakeholders to include not just investors, but also employees, customers, suppliers, communities in which it operates, and the environment, both now and into the future. It also requires making strategic and responsible decisions with both the short and long terms in mind. But pursuing social purpose goals may be complicated for US companies by the fact that under state corporation laws, companies owe their primary responsibility to shareholders. Therefore, companies generally need to demonstrate that pursuing these goals benefits shareholders as well as other stakeholders.

The corporate social purpose explosion

The latest uptick in social impact interest began during the 2016 proxy season, when there was a significant increase in shareholder proposals on social responsibility issues, making such proposals the second most prevalent proposals that year. The proposals related to diversity, climate change, wages (including gender pay equity), and equal employment. While most of the proposals generated only moderate levels of support, six proposals passed.[2] The trend continued in 2017, when even more social and environmental proposals were submitted (453, compared to 415 in 2016), including six that passed. Among the topics that generated increased interest in 2017 were matters affecting employees, such as gender pay equity (13 proposals in 2016 vs. 29 in 2017) and employment/discrimination (18 in 2016 vs. 43 in 2017).[3]

Several major "mainstream" investors are taking a new and prominent interest in social purpose as a *means* to sustainable, for-profit operations. There have been recent high-profile and significant calls to action, highlighting the need for CEOs to deliver both strong financial performance as well as positive social impact to be strong performers in the long-term.[4]

These major investors do not appear to represent isolated views; a 2017 study of institutional investor trust[5] yielded some surprising data, including that:

- Seventy-six percent of investors expect companies to take a public stand on social issues;
- Sixty-nine percent of investors care about how a company treats its employees; and
- Eighty-two percent of investors say trust is important when considering whether to invest in a company.

Perhaps in response to these expectations, companies have increasingly tried to demonstrate that they behave in a socially responsible manner, ultimately extending social impact beyond the corporate responsibility office or foundation and across the entire business. This process of true business integration has shifted the paradigm within many companies from responsibility to opportunity, with social purpose enabling new sources of shareholder value.

2. Deloitte, "On the board's agenda: The results are in—A review of the 2016 proxy season," August 2016.
3. Alliance Advisors LLC, 2016 and 2017 Proxy Season Reviews.
4. https://knowledge.insead.edu/blog/insead-blog/big-investors-call-for-company-attention-to-social-purpose-what-next-8451
5. Edelman 2017 study of institutional investor trust

Social purpose value proposition

Companies appear to increasingly recognize that corporate social purpose can be leveraged to facilitate value creation, competitive advantage, and other benefits that can add to the bottom line. Achieving these benefits can entail significant costs and effort; however, if successful, these efforts can strategically position a company to create value and compete more effectively with a wide variety of constituencies—consumers, employees, suppliers, communities where they operate, and investors, to name just a few. In fact, social purpose can create quantifiable business value on six key dimensions, including:

- **Brand differentiation:** Social impact initiatives may help companies boost their brands and achieve penetration in new markets.[6] Brands with a demonstrated commitment to sustainability are seeing average sales growth outperform brands without demonstrated commitment by fourfold.[7]
- **Talent engagement:** Companies with a strong social strategy tend to see higher employee engagement and have more success attracting and retaining talent. Employee engagement levels are shown to yield year-over-year increases in net income and earnings per share.[8]
- **Risk mitigation:** Companies have engaged in what are now called "social activities" to mitigate regulatory and social risks, and these activities are increasingly important today. Eighty-eight percent of consumers say they would boycott a brand due to irresponsible business practices.[9]
- **Innovation:** Identifying underserved social needs can be a strong driver of innovation, enabling companies to explore new models and technologies that might generate new market opportunities. Companies that are sustainability leaders are more than four times more likely to be recognized as innovation leaders in separate, independent rankings.[10]
- **Operational efficiency:** Operational efficiencies sourced from implementing more sustainable practices have been shown to save companies up to 45 percent in costs, with an ever-growing list of major companies seeing annual savings in the hundreds of millions.[11]
- **Access to market capital:** Companies with strong corporate social purpose see increased access to financing. The Morgan Stanley Capital International and KLD Research & Analytics, Inc. 400 Social Index is a market cap-weighted stock index of 400 publicly traded companies that have met certain standards of social and environmental excellence. Companies added to this index have realized a two percent average gain in share price, while those companies removed from the list have seen an average three percent loss.[12]

6. https://consciouscompanymedia.com/workplace-culture/hr-innovations/6-ways-corporate-social-responsibility-benefits-employees/
7. Nielson, "Sustainable Selections: How Socially Responsible Companies Are Turning a Profit," October 12, 2015.
8. Towers Perrin, "Employee Engagement Underpins Business Transformation," 2009.
9. http://www.conecomm.com/news-blog/2017/5/15/americans-willing-to-buy-or-boycott-companies-based-on-corporate-values-according-to-new-research-by-cone-communications
10. Deloitte, "Sustainability Driven Innovation: Harnessing Sustainability's Ability to Spark Innovation," 2013.
11. Forbes, "If Sustainability Costs You More, You're Doing It Wrong," 2012.
12. Devex Impact, "Is Corporate Social Responsibility Profitable for Companies?" February 20, 2013.
13. https://hbr.org/2014/07/sustainability-in-the-boardroom

The role of the board

Given these benefits, corporate social purpose has become a critical topic for governance and leadership consideration, and boards of directors have an important role to play. Boards have long understood their critical role of strategic and risk oversight. As the explosion of interest continues, and companies refresh their social purpose strategies and increase their commitments accordingly, boards may need to focus on overseeing both the nature of the commitment and the actions taken to implement it, as well as any risks that could arise from pro-social activities. Given the recent increased focus, the role of the board in this area is likely to develop and change in the coming years.

The role of the board is to oversee management. In this capacity, the board may want to ask management whether and to what extent the company has developed a social purpose strategy and the extent of related activities, challenge or question both, and review how they are being executed. If the company does not have a stated social purpose strategy the board may want to understand management's reasoning, challenging it as appropriate.

Depending upon the nature and extent of the company's social purpose, the board may wish to consider forming a separate, board-level committee to oversee those activities. Forming such a committee may generate reputational benefits by demonstrating the company's pro-social commitment at the highest levels. It may also provide some comfort to investors on board oversight of social purpose strategy, activities and related benefits and risks for the company. At the same time, boards may need to consider whether forming a new committee will put undue burdens on directors or employees responsible for assisting the board.[13] Whether or not companies form separate board-level committees, they should consider disclosing the role of the board in overseeing social purpose strategies and risks.

Whether within a sub-committee or under the purview of the entire board of directors, the board can also help management determine which issues and organizations should receive advocacy and support from the company. Just as the board oversees capital allocation, the board can oversee the allocation of the company's limited pro-social resources to help maximize shareholder value.

Questions for the board to consider:

Strategy

1. Does your company articulate a social purpose as part of its corporate strategy? If not, does your company have a social purpose strategy that exists elsewhere in the organization (i.e., Corporate Foundation)? If yes, is there an opportunity to align the social purpose strategy with the corporate strategy?
2. What are the costs? Can the company afford to incur these costs given limited resources?
3. What are the benefits? Should your company be doing more to publicize these activities and thereby gain added reputational benefits? Which of your stated business goals might be addressed through enhanced social focus and investment?

Competitive position

4. Where are your competitors focusing pro-social strategies and investments?
5. How does your company rank relative to others in your industry? By level of activity and engagement? By perception? What is your intended competitive positioning?
6. If and how are you communicating your social purpose strategy to key stakeholders?

Program portfolio

7. Which pro-social initiatives and investments does your company currently deliver? Which of these align to your business and operations?
8. If the benefits are significant enough, should your company expand these activities?
9. What process is used to determine how to allocate company resources to these activities?
10. Have the CSR activities been discussed with your institutional investors? What have they had to say on the subject?

Considerations & trends

Even companies with a strong commitment to social purpose face challenges and key strategic decisions in implementing their commitment. In addition, there are significant trends for boards to watch as companies determine how to activate a social purpose strategy.

- Companies are shifting from a siloed CSR view to a broader corporate social purpose strategy. The proper execution of a corporation's social purpose is likely to involve far more than traditional corporate philanthropy and takes into account the net impact of its business operations. For example, supporting diversity goes beyond financial donations to community organizations that empower diverse communities. It also involves hiring diverse employees, having a diverse board of directors, and mandating the use of diverse suppliers and other third-party vendors, including professionals such as accountants and attorneys. In addition, companies are increasingly integrating pro-social priorities into their core business strategy and reporting, more effectively communicating the impact, both social and financial, of social purpose activities by including social purpose information in corporate financial reporting.[14]
- One size does not fit all. The area(s) in which one company demonstrates its commitment to social responsibility may well differ—possibly significantly—from those that other companies address. Social purpose strategy and focus areas may depend on a wide range of factors such as brand identity, industry, size, location(s), resources, and history, including any history of noncompliance or other negative items that the company may want or need to overcome.
- Social responsibility activities may necessitate changes—sometimes fundamental changes—to core and other business practices. For example, responsible sourcing of materials can trigger significant changes in purchasing and procurement processes; responsible investing may require shifts in how potential investments are selected and how their performance is tracked; and encouraging increased diversity may necessitate reevaluating existing employee recruiting, hiring, training, and ongoing engagement practices.
- The tax changes enacted in 2017 have freed up funds that some companies are directing towards social-purpose initiatives. Several large companies have announced significant increases in corporate giving commitments directly tied to tax reform.[15]
- Companies are more frequently using their platforms to speak out on social issues, particularly those affecting their employees and their ability to do business, despite risks of alienating certain constituents and government officials. In a recent corporate survey conducted by the Committee Encouraging Corporate Philanthropy, six out of seven companies reported having a strategy for speaking out on social issues. In recent months, issues surrounding refugees and immigration, race and diversity, and gun violence have been particularly prominent, with CEOs, companies, and coalitions of companies increasingly taking public stands.[16]

As a result of these points and other factors, each company—with board oversight—should carefully consider evaluating its unique social purpose in the context of its core business strategy and which roles and actions are most authentic, advantageous and impactful.

Conclusion

Corporate social purpose has become a significant issue for companies, investors, and other constituencies. A company's role in society and the world at large can have positive impacts, ranging from reputational benefits with investors and others, to establishing sustainable business practices, to creating strategic marketplace advantages; however, these activities can also create risks. The board's oversight role with respect to strategy and risk should include overseeing the company's social purpose strategy, including encouraging management to address social purpose as part of its corporate strategy if it is not already doing so.

14. https://hbr.org/2018/04/the-right-way-for-companies-to-publicize-their-social-responsibility-efforts
15. https://www.bizjournals.com/sanfrancisco/news/2017/12/20/tax-reform-wells-fargo-bank-at-t-boeing-wfc-ba.html
16. http://cecp.co/leading-and-following-by-example-companies-taking-a-public-stance-on-social-issues/

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