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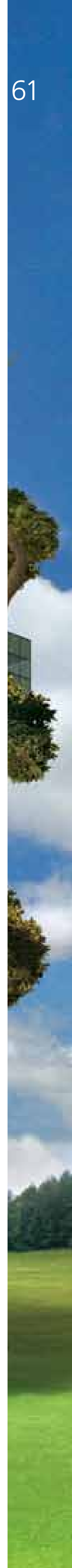
BY STEVE WAGNER, ERIC HESPENHEIDE AND KATE PAVLOVSKY
> ILLUSTRATION BY IGOR MORSKI



The *Responsible* and *Sustainable Board*

BY STEVE WAGNER > ERIC HESPENHEIDE AND KATE PAVLOVSKY
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Stressful times force hard choices: A company with declining revenues may curb corporate travel and lay off nonessential employees to ensure it has sufficient capital to remain a going concern. A "downsized" breadwinner may cancel cable TV and eschew dining out to scrape together enough money for mortgage and medical expenses.

But decisions made under duress are not always the most prudent, and things that may appear expendable during the heat of the moment may actually prove essential upon a more cool-headed examination. If a slumping company jettisons too much of its workforce, will it be able to capitalize on the next upturn? If a laid-off worker sells his car and cancels his Internet service, how is he going to find his next job?

Such may be the case with corporate responsibility and sustainability (CR&S). With companies fretting about credit, cash flow and revenue, CR&S issues may be the farthest thing from their minds. Yet the credit crisis hasn't fundamentally changed the dynamics around CR&S; it has only momentarily obscured them from view.

DEFINING CR&S

Companies addressing economic, social and environmental issues do so using various nomenclature, including:

- **Corporate social responsibility**
- **Corporate responsibility and sustainability**
- **Enterprise sustainability**
- **"Green" or "Greening"**
- **Corporate citizenship**
- **Environmental and social responsibility**

While the terms vary, they all generally refer to the same set of activities: strategically managing the social, environmental and ethical risks and opportunities of business.

Short-term concerns that demand the near-total attention of the executive should compel the board to address the longer-term issues around CR&S. If you, as a corporate board member, don't consider them, who will? If the issue goes unattended, what will be the consequences?

Here are a few reasons why CR&S should be on the board's radar screen, five from the negative side of the ledger and five positive:

Fear factors driving CR&S

1. ***Declining natural resources***. Oil, gas, water, minerals and other raw materials are being depleted, and the impact is already being felt at the pump, the meter and the cash register. Oil is particularly volatile: prices reached an all-time high of nearly $150/barrel in July 2008, only to tumble more than 50 percent by mid-October in the midst of the economic crisis.[1] While short-term volatility may continue, increasing demand from emerging economies such as India and China is expected to continue upward price pressure in the long term. Additionally, water quality and scarcity will become more prominent concerns in the near future, says the World Resources Institute.[2] Is your company prepared to pay dearly for what was previously cheap or free?

2. ***Imminent carbon levies.*** The days of blithely spewing carbon into the atmosphere are endangered, and smokestack industries will not be the only ones hard hit. Have you calculated the carbon impact of your corporate travel? Denmark, Finland, Norway and Sweden already have carbon taxes in place; Canada and other countries are actively considering them.[3] In the United States, the Obama administration has made a carbon cap-and-trade system a centerpiece of its environmental agenda; electric power, transportation fuels, commercial business and industrial business will likely be impacted.[4]

3. ***Discerning talent.*** According to a recent survey from Adecco, a human resources firm, 34 percent of Americans prefer to work for a company that "makes a conscious effort to promote socially and environmentally friendly practices," and 31 percent would be willing to take a pay cut to do so.[5] Do you have a CR&S strategy to attract future talent?

4. ***Aggressive competitors.*** Chances are at least one of your major competitors has taken a proactive approach to CR&S. According to a recent survey of 1,192 global executives conducted by the Economist Intelligence Unit,[6] 56.2 percent considered corporate responsibility a high or very high priority, compared with 34.1 percent three years earlier. Where does your company stand? Are your board and executives most comfortable moving ahead, keeping pace, or letting others lead? Do you know what your major institutional investors think of your CR&S activities?

5. ***Watchful entities.*** Increasingly, ratings agencies, proxy voting advisors, and corporate governance watchdogs are factoring CR&S issues into their assessments. Have you calculated the increased cost of capital that could result from a ratings downgrade?

Inspirational factors driving CR&S

6. ***Improving public image.*** A green halo can enhance a company's reputation and be a differentiator when it comes to making purchase decisions, both of your products and services and your company's stock. According to a 2008 Gallup environmental poll, 83 percent of respondents said they had changed their shopping and living habits over the last five years to help protect the environment.[7] Meanwhile, socially responsible investment funds now attract about one dollar out of every nine invested, according to Infinity Wealth Management.[8]

7. ***Mitigating risk.*** A thoughtfully implemented CR&S program can help you get and stay ahead of associated risk issues — reputational, financial, regulatory and legal. Recent business headlines (and court dockets) provide plenty of examples to inspire companies to improve performance, strengthen compliance and reduce risk around child labor, consumer product safety, food purity, environmental protection and other CR&S-related issues.

8. ***Reducing cost.*** Energy audits, process analyses, stakeholder surveys, capital improvements and other activities associated with a CR&S program can lead to reduced cost and increased efficiency. Consider, for example, just one small facet of CR&S — your company's office space. According to the U.S. Green Building Council, a new "green" building can yield 30–70 percent savings in energy use, 35–50 percent in water use, and 50–90 percent in waste costs.[9] Existing structures can be retrofitted at lesser savings.

9. ***Boosting strategy.*** Enmesh your CR&S program into your overall business strategy and the objective of each may be advanced. Companies in myriad industries have made their CR&S program synonymous with their corporate identities, including such global brands as Nike, Vodafone, Starbucks and others.

10. ***Making a difference.*** CR&S programs help change the tenor of business, from ruthless capitalism to capitalism with a face; from a bottom-line mentality to bottom-line plus; from a short-term mindset to a long-term vision.

REGULATION MAY FORCE YOUR HAND

Even if your organization is disinclined to tackle CR&S issues voluntarily, you may ultimately have no choice if, as expected, regulatory requirements take hold. Consider, for example, the area of greenhouse gas emissions. There are currently a number of economy-wide cap-and-trade proposals working their way through the U.S. Congress, with targeted greenhouse gas reductions of 70 percent or more below 1990 levels by 2050.[10]

On top of the national effort, significant greenhouse gas reduction initiatives have emerged on a regional level. For example, in North America, the eight-member Western Climate Initiative (made up of the U.S. states of Washington, Arizona, California, New Mexico, Oregon and Utah and the Canadian provinces of British Columbia and Manitoba) established a regional goal to reduce their greenhouse gas emissions to 15 percent below 2005 levels by 2020.[11]

Meanwhile, other CR&S areas may be poised for increased regulation, including environmental health and safety, materials bans, packaging and product labels,

SUSTAINABLE MOTIVATION?

In July 2008, Deloitte & Touche LLP presented a *Dbriefs* webcast entitled "Sustainability: A New Era for Enterprise Value?".[12] Attended by nearly 800 business executives, this webcast included polling questions on a variety of CR&S issues. One query addressed the primary motivation for companies' CR&S involvement.

"What is (or would be) the main objective for your company's sustainability efforts?"	
Increase revenue	19.9%
Enhance brand reputation	24.1%
Comply with regulatory and legal requirements	20.2%
Attract/retain environmentally conscious customers	5.3%
Become more attractive to talent	3.0%
It's the right thing to do	27.8%
Replies received: 773	

(Note: Due to rounding, total does not equal 100 percent. This is a nonscientific survey intended solely to track the opinions of webcast attendees. No effort was made to screen or qualify respondents to create a scientifically valid sampling.)

nano-technology, labor standards, recycling, and energy use. Organizations that anticipate and prepare for coming regulation may find themselves a step ahead; boards can promote and monitor such activity.

THE BOARD AS AUTO CLUB

While boards of directors can be powerful forces for good in an organization, there are, of course, limitations. Since they are not the ones driving the (hydrogen-powered) bus, directors, on their own, can't steer the organization along the CR&S roadway. The board's role is more akin to that of the automobile club: provide some maps; warn of potential hazards; offer advice; point out the landmarks; and be ready to provide roadside assistance if needed.

This advisory and oversight capacity may seem secondary to execution, but it is far from an insignificant task. In periods of economic stress, the wise counsel provided by the board can help ground an executive branch that is buffeted by the turmoil.

The board has the luxury of perspective that may be lacking at the executive level. Enmeshed in the day-to-day operations of the company, top executives often don't have the opportunity to step back and admire the vista. (And if they did, they'd probably notice a puff of smoke in the distance and rush off to put out the fire.) This perspective, and the knowledge that underlies it, may be the greatest asset that you bring to your organization as a board member.

SPURRING ACTION

In the realm of CR&S, where can the board add value and spur action? The opportunities are numerous, but here's one place to start: Sponsor a stakeholder survey. Find out what is important to those who make up and interact with your company, and use their input to help inform your CR&S program.

The CR&S world is a big place with almost limitless possibilities; your survey can help prioritize where your company can make the most viable, measurable, visible and relevant impact. As noted by the Commonwealth Institute, "a company in the fast food business probably has no real ability to fix the U.S. educational system. A retail clothing store probably can't solve world hunger."[13]

But before you take clipboard in hand, a reality check: The business community at large, and your company in particular, is not going to save the world. Global problems require global solutions, a broad-based effort involving governments, non-governmental organizations (NGOs), businesses and individuals. Not to say that you can't have an impact. It's just that your ambitions should be in line with your true capabilities. Each company has a role to play in CR&S, and for every company that role will differ. Planetary salvation may be out of the question, but improvement in your little corner of the world (and perhaps even the survivability of your company) is not.

So conduct or commission a survey of your customers, suppliers, employees, lenders, insurers, NGOs and, of course, shareholders. Include fellow board members, management team and business partners. Query analysts and consultants, your law firm, and your accountant. Poll your upstream and downstream supply chain. What are the values of these stakeholders? What issues do they care about? Aggregate and analyze their responses. The foundation, the rationale and the strategy for your CR&S activities can evolve directly from the survey results.

REFLECTION OF THE BUSINESS

From our work with and knowledge of dozens of successful CR&S programs, we have identified one commonality — acting in a strategically focused manner. So as you analyze your survey data, consider these questions: What should our company be known for? What are our greatest strengths? In what areas are we best positioned to make a mark? What is our long-term vision? What are our key growth strategies?

Many companies use their core business to help define their CR&S approach. For example, UPS, the global package delivery company, made delivery route efficiency a highlight of its CR&S initiative. The company used computer modeling to analyze thousands of delivery routes. Through this process, UPS was able to minimize left-hand turns (a source of both delays and accidents) and cut thousands of miles from drivers' itineraries. During 2006, the program cut 28.5 million miles off its delivery routes, reduced gasoline consumption by about three million gallons, cut carbon emissions by 31,000 metric tons, boosted safety, and earned hard-dollar savings for UPS.[14]

Other companies have extended their core identity into CR&S. Banco Santander, Spain's largest bank, developed a micro-credit lending program in South America. Through this initiative, low-cost business loans were offered to farmers, female entrepreneurs and other disadvantaged groups. Along with the loans, the bank sponsored workshops to train these budding executives in the art of sustaining and growing a business. The outcome transcends altruism: the bank expects that many of these growing businesses will maintain a profitable relationship with the bank.[15]

> SHISEIDO, THE JAPANESE COSMETIC COMPANY, LEVERAGED ITS EXPERTISE TO CREATE ITS SIGNATURE CR&S PROGRAM: ESTABLISHING A "SOCIAL BEAUTY CARE CENTER" THAT PROVIDES FREE ADVICE ON MAKEUP TECHNIQUES AND SKIN CARE TO INDIVIDUALS WITH "DEEP SKIN CONCERNS." CLIENTELE AT THE CENTER INCLUDE CANCER PATIENTS, PEOPLE WITH SKIN DISORDERS SUCH AS SCARS AND BIRTHMARKS, AND THE ELDERLY.

Shiseido, the Japanese cosmetic company, leveraged its expertise to create its signature CR&S program, establishing a "Social Beauty Care Center" that provides free advice on makeup techniques and skin care to individuals with "deep skin concerns." Clientele at the center include cancer patients, people with skin disorders such as scars and birthmarks, and the elderly.[16] Shiseido staff are also sent out to medical facilities and other institutions to help people with their skin care problems.

In each of these cases, the CR&S activities of the company were tightly integrated with the core business strategies. Boards should take the message to heart: A successful CR&S program will align with, reinforce and help propel the company's long-term

> ORGANIZATIONS THAT FAIL TO RECOGNIZE AND ACT ON CR&S ISSUES RISK ALIENATING THEIR OWN STAKEHOLDERS. IF YOUR CURRENT CUSTOMERS, PARTNERS, SUPPLIERS, WORKFORCE AND SHAREHOLDERS COME TO THE CONCLUSION THAT YOUR COMPANY IS DISREGARDING THEIR INTERESTS — AND, BY EXTENSION, THE INTERESTS OF SOCIETY AT LARGE — YOUR PROSPECT FOR RETAINING CURRENT AND OBTAINING FUTURE STAKEHOLDERS MAY BE ENDANGERED

vision and strategies. It will be a true reflection of the organization.

This principle can be applied to any business. An electric utility, for example, might make alternative energy the focus of its CR&S initiative; it could offer grants for small-scale solar and wind generation projects; promote the buy-back of excess capacity from these units; sponsor alternative energy science projects and fairs in the schools; offer free or low-cost energy audits to homeowners and businesses; provide scholarships for pursuit of science and engineering degrees; set up an energy demonstration project and invite schoolchildren to visit. These activities would support and enhance the company's core business and existing strategies; boost its reputation and standing in the community; demonstrate responsible and sustainable practices; and could positively impact the bottom line. Conversely, sending employees to clean city parks or paint classroom walls, while certainly laudable, would make significantly less sense from a strategic standpoint.

GET THE BOARD ON BOARD

How does oversight of CR&S fit within the board structure? To answer that question, Deloitte & Touche LLP recently sponsored a survey of 220 directors at American companies with $1 billion or more in revenues.[17] Directors were asked how their boards should organize to consider climate change and business sustainability issues. Just over one-third of respondents favored full board oversight, while another 37 percent indicated oversight should reside in existing board committees. When asked which committees should have this oversight responsibility, directors responded in equal numbers (24 percent each) that risk committees and governance committees should be in charge. Another 22 percent favored the strategy

GREEN OPPORTUNITIES

In the July 2008 *Dbriefs* webcast, "Sustainability: A New Era for Enterprise Value?,"[18] business executives identified abundant opportunities for generating CR&S value.

"Where do you see the highest potential for achieving value through sustainability in your organization?"	
Green IT/Data Centers	12.2%
Real Estate/Workplace	19.7%
Workforce/Grassroots 'Greening'	15.1%
Supply Chain	17.3%
Product Lifecycle	14.7%
Other	21.1%
Replies received: 763	

(Note: Due to rounding, total does not equal 100 percent. This is a nonscientific survey intended solely to track the opinions of webcast attendees. No effort was made to screen or qualify respondents to create a scientifically valid sampling.)

committee, and, likely to the relief of overburdened audit committee members, only 15 percent of directors wanted to assign responsibility to audit committees.

Since only a small minority of American boards have risk committees (which are most prevalent in financial services companies) or standing strategy committees, in many cases oversight should reside in the board governance (and nominating) committee. A number of recent proxy proposals calling for creating CR&S committees suggest that momentum to establish such committees will grow. However, establishing new board committees in the face of shrinking boards (11 was the average number of directors on S&P 500 company boards in 2007) and the growing oversight required of both audit and compensation committees may prove problematic.

THE GREENING OF THE BOARD

Taking the pulse of your stakeholders and getting the board properly structured are only two of many possible board activities. Here are some additional actions to consider:

Get board consensus: The need for a strong board role in CR&S has been acknowledged by many corporate governance advisors, including The Conference

Board of Canada[19] and the U.S. Business Roundtable.[20] Take the first step toward improving board performance by scheduling a retreat or creating a forum for the board to talk through CR&S issues. If disagreement arises, have a facilitated discussion that gets all the issues on the table and allows a consensus to emerge.

Emulate the strong: According to a 2008 study by The Conference Board of Canada,[21] companies with strong CR&S programs share certain characteristics, including tone at the top; developing CR&S commitments; establishing a CR&S committee; including CR&S metrics in CEO compensation; monitoring CR&S performance through regular progress reports; and including CR&S topics in new director orientation.

Ask the right questions of management: The board may want to verify that management is acting decisively on CR&S. This process starts with asking tough questions. Does your company have a "command center" to identify risks and opportunities associated with CR&S? Is this center supported with the right competencies — environmental engineering, legal, operational, marketing, controller, public relations and financing? Does your company have a roadmap for integrating CR&S into the operations of the business — with the appropriate governance structure in place?

Examine your footprint: Has the executive team determined the current environmental and social impact of your company — both good and bad? (Your internal audit department may be able to assist in this area.) You can't measure forward progress if you don't know where you are standing.

BETTING ON THE FUTURE

Notwithstanding all the upside and downside reasons for embracing CR&S, the board must first consider and always return to its primary fiduciary responsibility — to help govern the enterprise to attain long-term value creation.

Yet the phrase "long-term value creation" may be subject to interpretation. Does value creation include being a responsible member of society? Minimizing your negative impact on the environment? Doing right by your employees? Holding your suppliers and partners to high standards? Companies need to make these determinations themselves, and the responses will vary by organization. More important than the specific answers may simply be the act of asking the questions.

Organizations that fail to recognize and act on CR&S issues risk alienating their own stakeholders. If your current customers, partners, suppliers, workforce and shareholders come to the conclusion that your company is disregarding their interests — and, by extension, the interests of society at large — your prospect for retaining current and obtaining future stakeholders may be endangered.

On the other hand, if the board of directors can relieve the short-term stress on the executives by providing perspective and leadership on CR&S, this potential disconnect with your own stakeholders can be averted.

With CR&S, much is at stake. Don't let short-term uncertainty obscure the longer-term picture. The choices made now in this area will be felt by future generations.

Steve Wagner *is the managing partner for Deloitte & Touche LLP's Center for Corporate Governance and the innovation leader for its Audit and Enterprise Risk Services practice.*

Eric Hespenheide *is a partner in Deloitte & Touche LLP's Audit and Enterprise Risk Services practice.*

Kate Pavlovsky *is a principal with Deloitte Financial Advisory Services LLP*

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