

Making Corporate Social Responsibility Systemic

By Sarah A. Altschuller and Gare A. Smith

Consider the following three questions:

- Does your company have a corporate social responsibility (CSR) program?
- Does your CSR program manage risk for your company?
- Is it integral to the company's approach to risk management?

In response to the first two questions, many corporate leaders are likely to

answer "Yes." Many companies have adopted some form of CSR program, and many corporate executives recognize that CSR plays a role in managing both legal and reputational risks.

Unfortunately, despite a general understanding of the beneficial role that CSR can play in addressing risk, many companies are unable to provide an affirmative response to the third question. This is a problem, especially for multinational companies operating in diverse global environments, because it leaves them exposed to unnecessary risk.

A CSR program should be built into management standards and accountability mechanisms. It should be part of the company's overall business strategy, as understood and carried out by all managers, not just the few people with "CSR" or "Sustainability" on their business cards.

A strong CSR program can reduce the risk of lawsuits, divestment actions and boycotts. It also can mitigate the risks of negative news stories and other communications that have the potential to create long-term damage to a company's reputation with key stakeholders.

Companies are subject to the demands of a wide variety of stakeholders, including employees, shareholders, joint-venture partners, consumers, and the communities impacted by corporate operations. Increasingly, these stakeholders are advocating that companies manage the social and environmental impacts of their operations.

GOOD DEEDS ARE NOT ENOUGH

Many companies have responded to these pressures by adopting CSR programs that too often are just that – “programs.” They are not integrated into the overall management of the company's operation and relatively few personnel are held accountable for implementing CSR initiatives. Often, they are limited to philanthropic commitments, a few high-level policies, occasional public reporting, and a set of environmental and labor standards that are applied inconsistently across the company. This approach leaves a company with

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little capacity to develop strategic and comprehensive responses to stakeholder concerns.

Failure to understand the demands of stakeholders can be costly. For a large multinational, stakeholder opposition can lead to project delays or cancellations, additional conditions or costs associated with financing or insurance, and diverted staff time.

When these costs are quantified across a company's operations, the total can be surprisingly large. In his April 2010 report to the U.N. Human Rights Council, John Ruggie, the U.N. Special Representative on Business and Human Rights, reported that in his consultations with international extractive sector companies, he found that costly project delays often were the result of “stakeholder-related risks.” He noted that one company may have experienced a \$6.5 billion “value erosion” as the result of such non-technical risks.

There are significant risks for companies that claim to have embraced CSR and then, to demonstrate the degree of their commitment, simply point to glossy reports reflecting anecdotes and philanthropic initiatives. These companies fail to develop the internal policies and mechanisms necessary to ensure that the correct people, in the right functional areas,

are held accountable for following specific environmental and social standards. References to good deeds do not mitigate against the risks associated with lack of internal commitment and oversight.

Ultimately, CSR is about how companies are managed, not about the ways in which they choose to allocate certain profits through acts of philanthropy. CSR is about the core business functions of a company, and about being responsive to the ever-increasing demands of company stakeholders that companies be held accountable for the social and environmental impacts of their operations. The expectations of those stakeholders are expressed in forums ranging from traditional and social media and shareholder resolutions, to legislation and regulation, to disruptive protests.

CSR is, at its core, a strategic response to the changing nature of those expectations. Stakeholders increasingly expect companies to abide by a wide range of standards. Failure to respond to these expectations is risky, and companies should regularly assess them through a variety of channels.

Proposed shareholder resolutions, comments on social media channels, and community feedback through grievance mechanisms all provide important means for companies to assess stakeholder concerns. In particular, management personnel should consider the concerns that are raised by stakeholders with regard to a company's social and environmental performance.

Not all stakeholder concerns require a response in the form of a change in policies and procedures. Corporate managers are in the best position to make determinations about corporate policies. Collectively, however, stakeholder concerns provide, at a minimum, valuable intelligence about how a company's operations are perceived, and they should be thoughtfully and deliberately reviewed. The adequacy of a company's policies, standards, and internal accountability mechanisms should be assessed regularly, as should policies and procedures on stakeholder engagement.

Corporate stakeholders are raising concerns regarding an array of issues, ranging from corporate environmental performance to the impacts of company operations on indigenous communities. A significant focus of our practice is helping clients understand and respond to stakeholder concerns about the impact of corporate operations on human rights. Increasingly, companies are being held accountable to human rights standards established in international law.

SHAREHOLDER RESOLUTIONS

As one example of how stakeholders are raising concerns about human rights, during the 2010 proxy season investors filed resolutions with a number of companies, including Caterpillar, Hewlett-Packard, Motorola, and KBR, asking for the adoption of comprehensive human rights policies and assessment mechanisms.

The resolutions filed with Motorola and Hewlett-Packard urged these companies to develop policies sufficient to provide assurance that their “products and services are not used in human rights violations.” The resolution filed with KBR asked

the company to report on the extent to which its “contractors and suppliers are implementing human rights policies in their operations, including monitoring, training, [and] addressing issues of non-compliance[.]”

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Such resolutions are likely to increase in the coming years. Notably, in October 2009, the SEC issued a legal bulletin (Staff Legal Bulletin No. 14E) that reversed an earlier determination that had allowed companies to exclude shareholder resolutions requesting information on the financial risks associated with environment, human rights, and other social issues.

Shareholder resolutions provide an occasion for thoughtful internal and external dialogue about shareholder concerns. Early engagement on these issues can be critical, because when stakeholders perceive that companies are failing to address human rights concerns, it can lead to litigation or regulation.

For example, stakeholder advocacy has recently resulted in two legislative provisions that impose obligations on companies to assess the impacts of their operations on human rights:

- Section 1502 of the new Dodd-Frank financial reform legislation requires companies using minerals originating in the Democratic Republic of Congo or adjoining countries to report on their due diligence regarding the source and chain of custody of those minerals. This provision, meant to address concerns that the purchase of “conflict minerals” is fueling conflict in the DRC, is expected to impact companies in a variety of industries, ranging from consumer electronics and automobiles to jewelry and medical devices.

- The California Transparency in Supply Chains Act of 2010 requires retailers and manufacturers operating in California to disclose their efforts, if any, to “evaluate and address” the risks of human trafficking and slavery in their product supply chains.

NEW TERRAIN FOR DUE DILIGENCE

Both of these provisions create some new expectations with regard to due diligence. Raise the topic of due diligence in a room of corporate lawyers and you might expect that the conversation would turn to mergers and acquisitions or environmental site assessments. Increasingly, however, companies are being asked to apply due diligence strategies and systems to identify the human rights concerns that may be associated with their existing, or potential, operations.

Such developments in the law present challenges for companies, especially those that have not already engaged in an assessment of the human rights impacts of their operations.

It is important to recognize that many fundamental principles of international human rights law are already reflected in national law and regulation on safety, the environment, working conditions, anti-discrimination, and civil and political rights. With this understanding, corporate managers need not see stakeholder demands, or legislative requirements, regarding a company’s human rights performance as raising entirely new concerns. Demonstrating compliance with existing laws is a significant step in assuring stakeholders of a company’s human rights performance.

That said, in some contexts, stakeholders may be concerned about operations in a country with a relatively poor human rights records, where local laws may not be consistent with international law standards, or may not be enforced. Companies considering investments or operations in such countries are well-advised to consider the legal and reputational risks of their operations and to develop responses to those concerns.

Companies also are being asked to consider issues deep within their supply chains, and to demonstrate that they are making efforts to ensure that their sourcing practices do not lead to human rights abuses.

The legislative provisions and shareholder resolutions cited above are consistent with recent recommendations from the U.N. Special Representative for Business and Human Rights, urging companies to carry out “human rights due diligence”.

As framed by the Special Representative, human rights due diligence involves the implementation of policies, assessment mechanisms, internal oversight and control systems to identify,

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prevent, and address the actual and potential adverse human rights impacts associated with a company’s operations. Such mechanisms go well beyond the limited nature of the discretionary programs that continue to represent the approach of many companies to CSR.

The Special Representative’s framework on business and human rights is already influencing the policies and laws of a number of countries and multilateral institutions. For instance, the Organization for Economic Co-operation and Development (OECD) has cited to his framework in its Terms of Reference for the ongoing revision of its Guidelines for Multinational Enterprises.

A number of countries, ranging from the United Kingdom to South Africa, have recently cited the framework in undertaking their own policy assessments, and The European Parliament recently adopted a resolution that calls for a CSR clause in all European Union trade agreements. It would require companies to conduct due diligence to identify and prevent “violations of human and environmental rights, corruption or tax evasion, including in their subsidiaries and supply chains.”

These developments present both opportunities and challenges to companies. Compliance will not be simple. It is frequently hard to identify consistently reliable sources of information regarding, for example, the source of specific minerals or the veracity of supplier assurances regarding the status of certain workers.

What is clear is that these new expectations and requirements reflect a desire on the part of corporate stakeholders to ensure that corporate commitments to human rights go beyond short policy statements. Stakeholders increasingly expect companies to demonstrate that they have systems in place to evaluate, avoid, and mitigate the adverse impacts of their activities on human rights.

As companies assess this new environment, there is a major opportunity to adopt policies and procedures that are both responsive to stakeholder concerns and more effective at managing legal and reputational risks.



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