VIEW FROM THE TOP

How Corporate Boards can Engage on Sustainability Performance

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Anne Sheehan
Director of Corporate Governance, CalSTRS

FOREWORD

A unique dynamic exists between investors and board members. Directors are responsible for ensuring value for us, the shareholders. Yet, even the most patient investors must become involved these days in helping directors focus on the long-term. Because in an increasingly volatile, global, tech-driven, and competitive economic environment, short-termism often overwhelms planning for sustainable growth and returns.

Sustainability, though, is precisely where business needs to focus. Sustainability issues create risks, as well as meaningful investment and market opportunities. As investors, we have a responsibility to prepare corporate boards for this sustainability imperative.

At the California State Teachers' Retirement System, we have focused on the corporate governance of our portfolio companies for two good reasons: our investors deserve it and it produces results. As the nation's largest educators-only public pension plan in the U.S., we're the definition of long-term, patient capital. We see it as our duty to actively monitor and engage the investments in our portfolio for risks. Given the role of corporate boards in corporate planning and performance oversight, we pay very close attention to what the board is and is not doing on sustainability.

As long-term investors, we are looking for a company to be managed for resilience and sustainable growth. Investors can help develop informed board oversight of sustainability by assessing if directors have the appropriate sustainability expertise, encouraging directors to engage with stakeholders on sustainability priorities, and promoting the recruitment of diverse candidates capable of meeting the challenges of a diverse world.

If board directors are ultimately responsible to shareholders, institutional investors are ultimately responsible to our own investors. Our mandate is to ensure that we use every means possible to safeguard and increase the value of our investors' holdings. By being partners, activists, and analysts when it comes to board directors and sustainability, we can take a big step forward in delivering on that mandate.

Margaret Foran
Chief Governance Officer, Vice President and Corporate Secretary of Prudential Financial

FOREWORD

At Prudential Financial, we use the term sustainability to describe how we create enduring value. As a provider of life insurance, retirement and other investment products for our clients, having this long and broad view is crucial to our mission, and is an integral part of our business.

As the steward of our long-term value creation, our board has been a key driver of our commitment to sustainability. The Corporate Governance and Business Ethics Committee of our board oversees our sustainability efforts. The Committee receives regular updates on our progress towards sustainability and expertise in sustainability is among the skills represented on the board. Our board engages regularly with stakeholders, including investors, and the feedback and dialogue has resulted in changes to our governance approach.

Over the past several years, there has been an evolution in the understanding of the role of boards for sustainability. Traditionally, as part of their oversight duties, boards have focused on preparing for changes in the environment in which their company operates, as well as creating sustainable value for shareholders. More recently, best practices have included the board's oversight of including social and environmental risks into their company's overall business risk assessment and strategy.

The Ceres report "View from the top: How corporate boards can engage on sustainability performance" is both helpful and timely in this regard. With a combination of practical recommendations, and case studies, it will be a good guide for boards who want to better incorporate sustainability into their processes and action.

EXECUTIVE SUMMARY

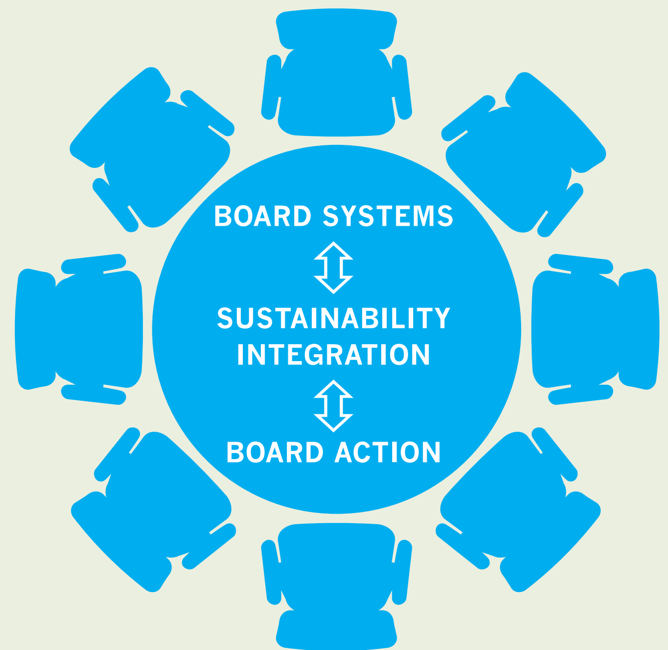
Today's corporations, faced with the extraordinary challenges of global climate change, water scarcity and workplace inequality, are at a crossroads. They can take proactive steps to adapt to pressing environmental and social issues – the two core categories of "sustainability" – or they can risk being left behind.

Sustainability is a critical business issue that all companies must focus on. Wall Street research, academic papers, corporate reports and trends from major investors all underscore the same message: companies that adopt sustainable practices deliver superior financial results and can face the future with more resilience.

Corporate boards must take a leading role in championing sustainability across the entire business enterprise. More than executives and other employees, members of corporate boards are responsible for ensuring long-term shareholder success and overall value creation. Directors have a duty and a mandate to promote sustainability priorities in corporate strategy, risk management and performance in order to meet this fiduciary responsibility.

Yet, while there has been a measurable uptick in director engagement on sustainability issues, it is still largely the exception rather than the rule among most companies. A 2014 Ceres analysis of 600 of the largest publicly traded U.S. companies found that only 32 percent oversee sustainability at the board level. Additionally, except in the case of a few leading companies, it is often unclear whether board sustainability oversight is achieving meaningful performance improvements.

Building on interviews conducted with dozens of corporate directors, senior corporate leaders and governance experts, this report identifies key strategies for effective board engagement that can produce tangible environmental and social impacts. **Specifically, the report recommends two inter-related approaches for weaving sustainability more deeply across board functions: 1) Integrating sustainability into board governance systems, and 2) Integrating sustainability into board actions. By combining robust systems and meaningful actions, boards will have a far better chance of achieving substantive performance improvements.**



TO DEVELOP ROBUST SUSTAINABILITY OVERSIGHT, CORPORATE BOARDS CAN:

- **FORMALIZE SUSTAINABILITY AS A BOARD PRIORITY**
- **INCORPORATE SUSTAINABILITY IN RELEVANT BOARD CHARTERS**
- **DEVELOP INFORMED SUSTAINABILITY OVERSIGHT**
- **ALIGN SUSTAINABILITY PRIORITIES WITH MANAGEMENT APPROACH, BUSINESS PERFORMANCE**
- **INCORPORATE SUSTAINABILITY IN STRATEGIC PLANNING**
- **INCLUDE SUSTAINABILITY IN RISK OVERSIGHT**
- **INCENTIVIZE MANAGEMENT FOR SUSTAINABILITY PERFORMANCE**
- **DISCLOSE THE ROLE THE BOARD PLAYS IN PRIORITIZING SUSTAINABILITY**

RECOMMENDATIONS

Among the report's recommendations for effective board sustainability oversight systems:

➲ **RATHER THAN CONSIDERING "SUSTAINABILITY" TOO BROADLY, FOCUS ON COMPANY-SPECIFIC MATERIAL ISSUES THAT SIGNIFICANTLY IMPACT OPERATIONS AND REVENUES.**

The most uptake of sustainability at the board level is in industries where environmental and social issues are well understood to pose regulatory or reputational risks. For instance, the 2013 Rana Plaza factory collapse in Bangladesh spurred board-level conversations about worker safety in the supply chain at a number of apparel companies. Additionally, companies are expanding board-level discussion of sustainability to include long-term business opportunities. *Unilever's* board is responsible for monitoring the implementation of the company's Sustainable Living Plan, its strategy for doubling their business while reducing their environmental footprint and improving their social impact.

➲ **EMBED SUSTAINABILITY IN COMMITTEE CHARTERS, AND IN DISCUSSIONS ON STRATEGY, RISKS AND INCENTIVES.**

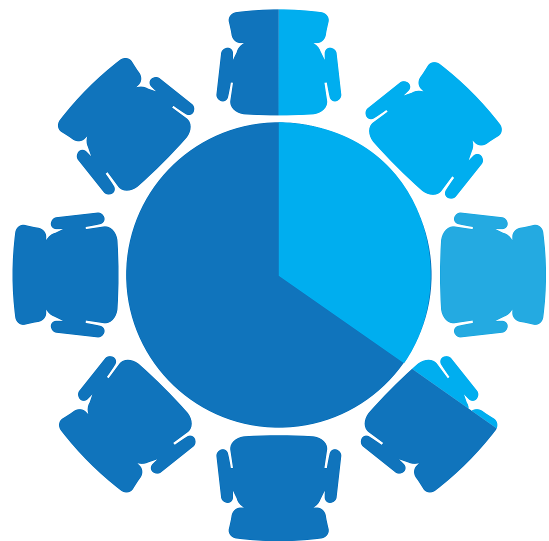
Integration in this manner is essential for ensuring that sustainability is not considered in a silo. *Gap Inc.* embeds sustainability into the mandate of its Governance Committee, which includes the Board Chair, and Chairs of the Compensation and Audit and Finance Committees, thereby allowing for both integration and meaningful dialogue.

➲ **RECRUIT DIVERSE CANDIDATES WITH EXPERTISE AND BACKGROUNDS ON KEY SUSTAINABILITY ISSUES AND OFFER SUSTAINABILITY TRAINING.**

Ceres found that only 19 percent of directors serving on board sustainability committees of large U.S. companies have discernible expertise in relevant issues. *Prudential Financial* identifies experience in "environment/sustainability" as a board qualification.

➲ **INVOLVE KEY STAFF RESPONSIBLE FOR ENTERPRISE PROFIT AND LOSS IN BOARD DELIBERATIONS ON SUSTAINABILITY.**

Management sets the framework for effective conversations at the board level by sharing the right information, and using board input to enhance organizational approaches on key issues. *Nike's* senior executives regularly appear before their Sustainability Committee to discuss how the sustainability and business strategies are aligned.



A 2014 CERES ANALYSIS OF **600** OF THE LARGEST PUBLICLY TRADED U.S. COMPANIES FOUND THAT ONLY **32** PERCENT INCORPORATE SUSTAINABILITY AT THE BOARD LEVEL

Recommendations for board action towards stronger sustainability performance improvements:

- **AVOID OVER-EMPHASIS ON SHORT-TERM RETURNS BY EMBEDDING SUSTAINABILITY AND LONGER-TERM THINKING IN STRATEGIC PLANNING.**

  Boards have the responsibility to move company leadership away from a preoccupation with quarterly earnings targets, and should focus instead on planning for long-term performance. A growing number of company boards, including *Coca Cola*, *Unilever* and *National Grid*, have taken steps to move away from quarterly reporting. Intel has explicitly noted the board's responsibility on "long and short-term trends," while *Prudential Financial's* board considers a "long-term value creation model."

- **INTEGRATE SUSTAINABILITY IN RISK OVERSIGHT.**

  Boards are responsible for systematically reviewing corporate exposure to material sustainability risks and scrutinizing management strategies to mitigate risks. *Marks and Spencer's* board regularly reviews a group risk profile in which environmental and social issues are identified as contributing to broader risks, such as reputation and supply chain risks.

- **ESTABLISH STRONGER LINKAGES BETWEEN EXECUTIVE COMPENSATION AND SUSTAINABILITY GOALS.**

  Only 25 percent of large U.S. companies link executive compensation with sustainability issues. *PG&E* links 50 percent of the short-term compensation of its executives to its safety performance.

- **DISCLOSE THE ROLE OF THE BOARD IN PRIORITIZING SUSTAINABILITY.**

  While integrating sustainability in board systems and actions is important, it is also crucial for companies to provide robust disclosure on board sustainability oversight. In addition to helping investors and other stakeholders gauge such activity, better disclosure will also allow stakeholders to identify linkages between robust accountability systems and sustainability performance impacts.

"The Board should be the first line of defence against the dominance of short-term thinking by a company. While management tends to be focused on the crisis of the moment, it is the responsibility of the Board to ensure that company leaders also give due attention to the next five years and beyond."

— IAN DUNLOP
Independent Adviser & Commentator - Climate & Energy, former CEO Australian Institute of Company Directors and Chair Australian Coal Association

INTRODUCTION

The findings of reports from the World Economic Forum[1] and other sources[2] are clear: “business as usual” cannot be sustained. Our world faces significant environmental and social risks that will profoundly shape economic stability and security. Despite this reality, most companies have still only made limited progress in addressing these risks in their planning and decision-making. Organizations that do recognize the impact of sustainability issues on their business and make the necessary adjustments to corporate strategy and approach will be better positioned for long-term success and value creation for sustainability. There is a clear need for corporate leadership that encourages action and boards of directors, responsible for overseeing the interests of shareholders in the long-term, have a critical role to play.

This report provides detailed analysis on the role of corporate boards to oversee, champion and drive sustainability within an enterprise. Included within are:

- Tactics for how companies can organize boards to oversee sustainability in a thoughtful and engaging manner;
- Strategies for how directors can leverage their roles and take action to orient a company towards sustainability performance results; and
- Recommendations and examples that can be used by directors, company executives and investors to assess how board sustainability oversight could be exercised in an effective manner.

THE BACKGROUND: GROWING INTEREST AMONG INVESTORS

Research and analysis from the Harvard Business School,[3] University of Oxford,[4] Deutsche Bank[5] and many others underscore the connection between sustainability and long-term corporate performance, consistently demonstrating that companies that embrace sustainability in their systems and strategies outperform their peers on a variety of crucial financial metrics.

Investors are increasingly aware of these correlations, recognizing that sustainability issues not only pose financial risks but also provide opportunities for investment. Between 2012 and 2014, total assets under management using socially responsible strategies expanded in the U.S. to $6.57 trillion from $3.74 trillion, an increase of 76 percent,[6] and accounted for over $21.4 trillion globally.[7] Large institutional investors, in particular, are beginning to step forward. Norway’s sovereign wealth fund, the largest in the world, plans to double its investments in sustainability[8] and in 2014, divested from 114 companies, including 32 coal mining companies, citing risks related to climate change.[9] In 2012, CalPERS, the largest public pension fund in the U.S., set a goal of integrating sustainability across its entire investment portfolio.[10]

Investors are increasingly focusing on the role that corporate boards play in overseeing material sustainability issues as a part of their fiduciary responsibility. The Sustainable Investment Institute (SI2) notes that between 2010 and 2014, over 250 shareholder resolutions were filed calling for explicit board oversight of sustainability issues.[11]

BOX 1: CERES ROADMAP AND CORPORATE ASSESSMENT REPORTS

The 2010 report, ***Ceres Roadmap for Sustainability*** recommended that boards of directors provide oversight on corporate sustainability strategy and performance with this responsibility specifically included in a committee charter.

Twice since the Roadmap's publication, Ceres has partnered with research firm Sustainalytics to assess the performance of 600 large U.S. companies relative to the Roadmap expectations, including Board Oversight.

The 2012 report, ***The Road to 2020: Corporate Progress on the Ceres Roadmap to Sustainability***, found that while board oversight of sustainability can take several forms, it was the scope and ambition of the board's mandate that was most relevant to performance. This mandate could include company-wide oversight of issues, such as climate change, human rights, sustainable supply chain management and health and safety, as well as sustainable products and services.

The 2014 report, ***Gaining Ground: Corporate Progress on the Ceres Roadmap for Sustainability***, showed that leadership in board sustainability oversight was coming largely from heavy industries, such as utilities and materials firms with significant exposure to environmental and social risks. While board committee charters help to formalize board oversight, the study also noted that companies were starting to engage their boards on sustainability in less formal ways.

Ceres Roadmap for Sustainability. *The Ceres Roadmap for Sustainability*[12] lays out 20 expectations for corporate accountability systems and performance on sustainability. Among these, Ceres calls on corporate boards to provide oversight and accountability for their companies' sustainability strategies and performance. In 2012 and 2014, Ceres released reports assessing 600 of the largest publicly traded U.S. companies on their performance against the Roadmap's expectations. The assessments found that, while an increasing number of businesses are incorporating sustainability at the board level, rising to 32 percent in 2014 from 28 percent in 2012, those who do so are still in the minority. Also, except in the case of a few leading companies, it is unclear what level of influence board oversight has had over sustainability performance results.[13]

"Investing in innovation and future production, developing talent and ensuring robust supply chains are among the many Environmental, Social and Governance (ESG) related management actions that enhance a company's ability to generate long-term financial returns. Businesses that fail to make sufficient investments in the future can doom themselves to irrelevance."

— LARRY FINK
CEO of Blackrock, 21st Century Engagement: Investor strategies to incorporate ESG considerations in corporate interactions

Drawing connections between board sustainability oversight systems and sustainability performance can be difficult for a number of reasons. For instance, a business may lack the knowledge needed to structure board oversight so that it is focused on sustainability performance results. A company may put superficial, or token, systems in place to satisfy external stakeholders.[14] A lack of transparency in how the board functions may also make it difficult to determine when oversight on sustainability is being exercised effectively.

Given the focus of Ceres and our partners in advocating for effective accountability systems that lead to positive environmental and social performance impacts, it is important to develop clarity on how board sustainability oversight should be exercised. This report lays out two ways that this could be approached. The first approach includes recommendations for how sustainability can be incorporated into board systems and processes, thereby ensuring that key issues are considered systematically and as a part of standard governance processes. The second outlines specific tactics for boards and individual directors to take advantage of opportunities for action that build on the structures being put in place. **Ceres believes that it is the combination of robust systems and responsible action that will lead to meaningful sustainability performance improvements.**

METHODOLOGY

The research process for this report builds on important work by a number of organizations, including Calvert Investments, the National Association of Corporate Directors, the United Nations Environment Programme Finance Initiative, Sustainable Investment Institute, the UN Global Compact and The Conference Board, among others.

Confidential interviews with corporate directors, senior corporate leaders and governance experts were critical in developing the recommendations and generating examples. The interviews were customized to gain insight from the individual participant's experience, but focused on the following overarching questions:

- What does effective board oversight for sustainability look like?
- How can board oversight be structured in a way that leads to sustainability performance improvements?

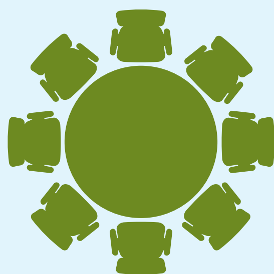
In this report, sustainability is defined as economic, social, and environmental issues that affect corporate strategy and performance over the long term.

The report focuses primarily on U.S. companies and builds on the research and analysis laid out by *Ceres in the Ceres Roadmap, Road to 2020*, and *Gaining Ground reports*.

The report is designed to be useful primarily to directors interested in enterprise sustainability priorities and executives looking to engage corporate boards on these issues. The analysis could also be useful to investors and other stakeholders who want to assess how a company is being governed for sustainability. The recommendations will be relevant to companies at various stages in their sustainability integration journey. This is a first step in Ceres' exploration of board sustainability oversight and identifies multiple areas where further research and engagement is required.

INTEGRATING SUSTAINABILITY INTO BOARD SYSTEMS

This section lays out strategies for how sustainability could be woven into corporate board systems and processes in order to institutionalize effective and robust consideration of these issues. The approaches suggested should be tailored keeping in mind a firm's size, corporate culture and strategic and operational priorities.



MAKE SUSTAINABILITY A FORMAL BOARD PRIORITY

To encourage the board to prioritize sustainability, companies can:

- **Identify specific environmental and social priorities.**
- **Establish clear connections between sustainability priorities and corporate risk and revenue.**
- **Emphasize long-term performance**

Since sustainability influences a corporation's ability to create and maintain value, directors and management should proactively create opportunities for corporate boards to consider relevant sustainability issues in a substantive manner.

This is easier said than done as board agendas become increasingly crowded. A February 2014 report by McKinsey and Company notes that "[d]irectors still spend the bulk of their time on quarterly reports, audit reviews, budgets, and compliance—70 percent is not atypical—instead of on matters crucial to the future prosperity and direction of the business."[15]

For sustainability to become a board priority, it is critical to go beyond addressing sustainability as an "extra-financial" issue. Instead, companies should clarify linkages between sustainability and revenue and risk. Investors can play a key role in reinforcing this connection by raising sustainability in their corporate engagements. The report *21st Century Engagement: Investor Strategies for Incorporating ESG Considerations in Corporate Interactions*[16] lays out a number of effective strategies for doing this.

Identify specific environmental and social priorities. Several interviewees for this project emphasized the importance of prioritizing specific issues when making the case that sustainability belongs on the board agenda. Rather than considering "sustainability" writ large, board deliberations should focus on material environmental or social issues that significantly impact operational and business function. Material issues could be identified through formal processes run by management to identify sustainability priorities,[17] quantitative and qualitative analyses, as well as enterprise risk management systems. The emerging understanding that sustainability issues pose business risk points to the further integration of these processes in the future.

> "At the end of the day, 'sustainability' is a proxy word. One of the ways to engage board members and staff on the financial side of a company is to identify specific sustainability issues that pose business risks."
>
> **— DIANNE DILLON RIDGELEY**
> former Board member from Interface and GME at the 2015 Green Biz Conference

While it is important to focus on specific sustainability issues, interviewees also noted that the board should not consider these issues in a silo. Most environmental and social issues are interrelated and should be considered as such.

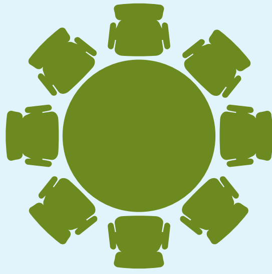
Establish clear connections between sustainability priorities and corporate risk and revenue. The links between sustainability and risk are best recognized in heavy industries, such as the oil and gas, electric power and materials sectors, where the impact of environmental and social issues are often better understood and are the focus of regulatory and compliance rules. In fact, Ceres' *Gaining Ground* report found that these sectors demonstrate the highest proportion of explicit board oversight systems for sustainability.

In other industries, we found that reputational risk is the primary factor motivating corporate boards. For example, the 2013 Rana Plaza factory collapse in Bangladesh spurred board conversations about worker safety across the supply chain at a number of apparel companies. Since the branding and competitive differentiation of apparel companies relies in large part on consumer perception, clothing firms are highly motivated to address these risks throughout the enterprise, starting with leadership and oversight from the board of directors.

Interviewees noted that the competition for talent is motivating a number of corporate boards to monitor and improve their enterprise sustainability reputation. In a nationwide survey of students and new employees, Net Impact found that 45 percent of respondents stated that they would be willing to take a 15 percent pay cut for "a job that makes a social or environmental impact."[18]

Leading companies are also expanding board level discussion of sustainability to include long-term business opportunities. For example, *Unilever's* Sustainable Living Plan lays out the company's effort to double the size of its business by 2020, while reducing its environmental footprint and improving social impact.[19] *Unilever's* board is involved in reviewing the implementation of the Sustainable Living Plan. The board Corporate Responsibility Committee monitors the progress – and potential risks – of the Sustainable Living Plan and reports back to the overall board. The Audit Committee oversees the independent assurance of the Plan.[20]

Emphasize long-term performance. Because corporate boards and management are typically under tremendous pressure to demonstrate short-term returns to investors, making the case for longer-term sustainability performance can be difficult. In fact, a 2014 McKinsey survey of corporate executives and directors found that the board of directors was primarily responsible for an organization's overemphasis on short-term financial results.[21] Intel has addressed this issue by explicitly noting the board's responsibility to deliberate on "*long and* short-term trends and impacts to our business from environmental, social and governance issues" in its Nominating Committee Charter.[22] *Prudential Financial's* 2013 Proxy Statement included a "long-term value creation model," which was intended, in part, to jumpstart the conversation on long-term performance among the board, company management and shareholders.[23]



FIND A HOME FOR SUSTAINABILITY ON A BOARD COMMITTEE

To institutionalize sustainability in board committees, companies can:

- **Add references to sustainability priorities in committee charters.**
- **Integrate sustainability considerations into committees responsible for strategy, risk, and incentives.**

The *Gaining Ground* report noted that a small, but growing number of companies are starting to engage their boards on sustainability informally through occasional presentations and updates. While this is an important first step, Ceres recommends that boards put in place formal processes for sustainability. This will help ensure that critical environmental and social issues are considered systematically as a part of board deliberations and decision-making.

Add references to sustainability priorities in committee charters. Directors and management can establish a formal foundation for sustainability at the board level by writing specific language into relevant board charters. For example, in response to shareholder dialogue, in 2010, *Intel* expanded its Board Governance and Nominating Committee charter to include explicit reference to "matters of corporate governance and corporate responsibility, such as environmental, sustainability, workplace, and stakeholder issues."[24] Investors referencing this change cited a legal opinion that noted that charter incorporation generates a fiduciary obligation on directors to attend to these issues.[25]

BOX 2: APPROACHES TO INCLUDE SUSTAINABILITY IN BOARD COMMITTEE CHARTERS

Companies could incorporate sustainability in committee charters by:

- **Identifying sustainability priorities**: *Citi's* ***Public Affairs Board Committee charter*** identifies "environment, climate change and human rights" as areas of focus.
- **Noting specific oversight responsibilities**: *Sysco* ***Corporation's Sustainability Committee*** is explicitly charged with the responsibility to review management's risk assessment and risk management policies and procedures with respect to sustainability. *HSBC's* Board Corporate Sustainability Committee is tasked with the responsibility of reviewing and advising the Board on the Group's sustainability targets. The Committee also examines and approves the Group's environmental performance and impacts. Many Board committees with sustainability responsibility are also charged with reviewing the enterprise's sustainability disclosures.
- **Making the link to business**: *Ford's* ***Sustainability and Innovation Committee charter*** clearly states that the "principal functions" of the committee will focus on motor vehicle customers, government regulation on motor vehicle and stationary source emissions, daily business activities and new and innovative technologies.

Additional resources: The 2014 National Association of Corporate Directors report ***Oversight of corporate sustainability activities*** includes a model charter for corporate sustainability committees that addresses purpose; membership; duties and responsibilities; performance evaluation; and structure and operations.

"We view the oversight role of a company's board as consistent with our own investment beliefs that long-term value creation requires strong governance along with effective management of environmental and human capital factors."

— ANNE STAUSBOLL
CEO, California Public Employees Retirement System

Integrate sustainability considerations into committees responsible for strategy, risk, and incentives. To date, companies have structured board sustainability oversight in three broad ways:

- A dedicated committee for sustainability issues;
- Sustainability integrated into the mandate of an existing committee, typically through charter reference; and,
- Sustainability as the responsibility of the entire board of directors.

Ceres believes that there is no "one size fits all" solution to structuring sustainability oversight at the board level. Establishing a stand-alone board committee for sustainability creates a dedicated forum for discussing environmental and social issues regularly and in depth. However, this approach carries the risk of separating sustainability from dialogues on strategy and finance. Including sustainability in the mandate of existing committees would help integrate these issues into traditional business functions. But this could again deter in-depth conversations about sustainability issues, especially when the issues cannot be directly linked to short-term risk, revenue, and reputational considerations. While designating sustainability as the responsibility of the board at large can help give these issues prominence within the organization, the time needed to delve into sustainability issues may be lost through this approach. The board and management need to make a choice on specific committee structures based on appropriate levels of dialogue, regular and systematic time allocation, and issues of focus for the short and long-term benefit of the company.

BOX 3: DISTRIBUTION OF SUSTAINABILITY OVERSIGHT AMONG CORPORATE BOARD COMMITTEES

In its 2014 report ***Board Oversight of Sustainability Issues***, which assessed 277 U.S. companies with dedicated sustainability oversight, Sustainable Investment Institute analyzed which board committees had been charged with sustainability oversight. Approaches include the following:

- 32 percent address sustainability though a dedicated committee;
- 34 percent consider sustainability in their nominating/governance committee;
- 10 percent consider sustainability in the audit committee;
- 1 percent consider sustainability through the risk committee; and
- 13 percent tie sustainability to committees with other oversight roles, such as technology, product, innovation and compensation.

Regardless of where sustainability is housed on the board, Ceres recommends that companies set up systems to enable cross-pollination of sustainability-related discussions with the committees responsible for strategy, compensation and risk management.

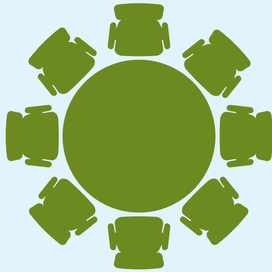
Gap Inc. provides an interesting example of how a company's board oversight structure can evolve. The company housed sustainability oversight first at the committee level and then with the board at large. In 2014, the company integrated sustainability into the mandate of its Governance Committee, now called the "Governance and Sustainability Committee." Since this Committee includes the board chair, the chair of the Compensation Committee, and the chair of the Audit and Finance Committee, and its meetings involve the CEO and Corporate Secretary, this solution holds promise for both integration and depth of dialogue.

BOX 4: INTEGRATING SUSTAINABILITY INTO EXISTING BOARD COMMITTEE RESPONSIBILITIES

The 2014 UNEP FI report ***Integrated Governance: A new model for governance for sustainability*** lays out how different board committees can incorporate sustainability into their functions:

- *Governance committee*: Oversee sustainability trends and their impacts on the business; Introduce director training for sustainability; Review corporate policies on sustainability
- *Audit committee*: Understand risks and opportunities relating to reporting the sustainability performance of the firm; Ensure quality and timeframe of sustainability and other corporate disclosures; Monitor research and development on sustainability; Ensure compliance with new regulations on sustainability.
- *Compensation committee*: Link material sustainability issues to ESG targets; Integrate sustainability executive performance evaluations and compensation; Engage with investors on sustainability and compensation.
- *Nominations committee*: Integrate sustainability into the director nominations process; Integrate sustainability into board performance evaluations.

REGARDLESS OF WHERE SUSTAINABILITY IS HOUSED ON THE BOARD, CERES RECOMMENDS THAT COMPANIES SET UP SYSTEMS TO ENABLE CROSS-POLLINATION OF SUSTAINABILITY-RELATED DISCUSSIONS WITH THE COMMITTEES RESPONSIBLE FOR STRATEGY, COMPENSATION AND RISK MANAGEMENT.



DEVELOP INFORMED OVERSIGHT OF SUSTAINABILITY

To craft boards that can exercise informed sustainability oversight, companies can:

- **Include relevant expertise in board skills matrices.**
- **Recruit diverse candidates with critical skills and expertise.**
- **Offer training on sustainability issues.**
- **Make time on the board agenda and provide the right materials for thoughtful sustainability discussions.**
- **Encourage directors to engage with stakeholders on sustainability priorities.**
- **Evaluate board performance on sustainability oversight.**

After establishing sustainability as a board priority and finding a home for these issues at the board level, companies should set up systems to ensure that the issues in question are considered in a thoughtful and informed manner. Directors need to have sufficient background on key issues to support, question and offer meaningful advice to management.

Include relevant expertise in board skills matrices. Directors and management should assess the qualifications and expertise of current directors and map this against the company's sustainability priorities. Many nominating committees conduct formal gap analyses when identifying potential new board candidates. Where a sustainability issue is identified as a material priority and board focus, the nomination process should involve the consideration of expertise in the issue in question as a part of a skills matrix.[26]

Prudential Financial includes a board skills matrix in its annual proxy statements.[27] The matrix identifies experience in sustainability as a board qualification, noting that "environment/ sustainability/ corporate responsibility strengthens board oversight and assures that strategic business imperatives and long-term value creation for shareholders are achieved within a responsible, sustainable business model."[28]

> WHERE A SUSTAINABILITY ISSUE IS IDENTIFIED AS A MATERIAL PRIORITY AND BOARD FOCUS, THE NOMINATION PROCESS SHOULD INVOLVE THE CONSIDERATION OF EXPERTISE IN THE ISSUE IN QUESTION AS A PART OF A BOARD SKILLS MATRIX.

BOX 5: INCORPORATING SUSTAINABILITY IN A SKILLS MATRIX

The report ***Towards a Sustainability Mindset***, released by Business in the Community, identifies the following sustainability components that could be included in a board skills matrix:

For all board members:

- Basic awareness of sustainability, its importance to the company and the business case for sustainability at the company;
- Ability to recognize the most basic sustainability impacts of the organization, and how poor sustainability performance can have a negative effect on the company's reputation and brand;
- Capacity to articulate how sustainability relates to the company's vision and strategy; and
- Understanding of sustainability trends as they affect the market segment.

For at least one director:

- Understanding of how companies can embed sustainability;
- Familiarity with individuals and groups working in the field;
- Experience with board oversight of corporate sustainability;
- Knowledge of how to create and implement metrics for corporate sustainability; and
- Ability to engage with stakeholders, make use of their advice and manage public commitments toward sustainability.

Recruit diverse candidates with critical skills and expertise. Once companies identify the sustainability skills that their board should have, every effort should be made to recruit a diverse group of individuals with those abilities. This includes pinpointing and bringing on experts in key issues where relevant, and assessing the sustainability knowledge of all potential directors.

This emphasis on board diversity, covering gender, ethnicity, background and experience, has long resonated with investors, who see this as a key component of board quality and good governance. Research shows that diverse groups examine more alternatives and often do so more fairly than homogenous groups, helping avoid "group think."[29] Socially responsible investors, led by Calvert Investments, Pax World Funds, and others, are creating a robust movement that calls for more gender diversity on corporate boards. The movement is gaining momentum, propelled by research from Thomson Reuters,[30] Catalyst[31] and others showing that companies with women on their boards outperform their peers on a host of financial metrics.

A number of investors are starting to call for the inclusion of directors with expertise in critical environmental and social issues on corporate boards[32] and to take action against companies whose boards do not reflect the appropriate expertise. The recently launched Boardroom Accountability Project,[33] which calls for "diverse, independent and accountable directors," has submitted proxy access proposals to over 75 companies with a focus on climate change, board diversity and excessive CEO pay. The effort was initiated by the New York City Comptroller's Office and involves many large institutional investors.

At the 2014 Duke Energy Annual meeting, following a coal ash spill, CalPERS and the New York City Comptroller's office urged shareholders to vote against members of the company's board Regulatory Policy and Operations committee for "failing to fulfill their obligations of risk oversight."[34] In a joint statement, the investors argued that given the major risks that energy companies face, environmental risk management is a critical area for independent board oversight. The statement called for Duke Energy to conduct a review of their boards skills and expertise and to bring on to the board "fresh talent with experience and deep knowledge of the coal industry, environmental risk and relevant regulatory expertise."[35]

In spite of these efforts, the number of experts in sustainability issues sitting on corporate boards remains low. Ceres commissioned detailed analysis of the make-up of relevant board committees in companies that had explicit sustainability oversight in place, as identified by the *Gaining Ground* report. The analysis revealed that of the 774 directors who sit on such committees, only 19 percent have discernible or specific sustainability expertise in environmental, social or governance issues, as described in their biographies on corporate web sites or in the nominating discussions in proxy statements.

A number of interviewees noted that boards should recruit individuals with a combination of sustainability, business and industry expertise so they can advance a perspective that integrates these components. Yet, even when companies are interested in appointing directors with the relevant expertise, a common perception remains that it can be difficult to find individuals with the right skill sets, and some stakeholders noted that this poses a particular challenge for smaller companies. Initiatives, such as the Diverse Directors Datasource,[36] have emerged to fill gaps in this regard.

Offer training on sustainability issues. Boards and management should provide training opportunities on sustainability priorities to the entire board or members of relevant committees. A number of companies have put in place formal and informal systems to educate directors on key sustainability issues.

Increasingly, companies are raising awareness about sustainability by inviting non-profits, peers and other experts to present to the board on broad and specific sustainability topics. Ceres engaged with a number of corporate boards in this way, building on the structure provided by the Ceres Roadmap for Sustainability. The UN Global Compact LEAD program also launched a set of training modules on sustainability.[37] Groups focused on director training, such as the National Association of Corporate Directors and The Conference Board, are also working on sustainability. Formal and informal director peer groups could also be leveraged to exchange best practices and ideas.

The Co-operators offers dedicated sustainability training to its entire board annually.[38] The Sustainability and Citizenship Committee identifies the training topics and organizes sessions that typically include external speakers with sustainability expertise. Additionally, the organization offers directors a budget for education/ training and identifies sustainability related courses that directors could consider.

Make time on the board agenda and provide the right materials for thoughtful sustainability discussions. Boards and management should create opportunities for key sustainability issues to be discussed regularly and in depth, instead of wedging them into a larger agenda. Additionally, boards should work with management to ensure that materials are furnished that will enable informed discussions. These materials could include details on management's plans or strategy regarding specific sustainability issues, potential corporate goals, peer comparisons and benchmarks.

There may be times when directors need to jumpstart the conversation of sustainability with management. In such circumstances, directors should work with board chairs, independent chairs and committee leaders to include the consideration of key sustainability issues in board meeting agendas, thereby ensuring that management charged with presenting to the board become engaged on the topic.

BOX 6: QUESTIONS THAT BOARDS SHOULD ASK ON SUSTAINABILITY

In jumpstarting a conversation on sustainability, boards could ask the following questions based on Ceres Roadmap for Sustainability expectations:

- **Materiality**: What are our sustainability priorities and how were they identified? Are these priorities financially relevant to investors in the short- and long-term? Were stakeholders engaged in identifying these priorities?
- **Strategy and risk management**: How have the sustainability priorities been factored into the strategic plan and risk management process? How are emerging issues being identified?
- **Disclosure**: Have sustainability priorities and their impacts on the strategic plan been disclosed to stakeholders in a complete, comprehensive and credible manner?
- **Performance**: What goals have we set to improve our performance on our sustainability priorities? How do these compare with the goals set by our peers? Do these goals set us up for leadership in our industry?
- **Scope**: Do the sustainability goals cover our significant impact areas, including operations, supply chains and products?
- **Employees**: What is our strategy to build our employee base to meet our sustainability priorities?
- **Compensation**: Do we have the right incentives in place for management to meet sustainability priorities and goals?
- **Governance**: Have we established a governance structure that allows the board to oversee the management of sustainability issues and their integration throughout the enterprise?

Additional resource: In their report, ***Sustainability: Questions for Directors to Ask***, the Chartered Professional Accountants of Canada provide a briefing for directors on sustainability, and lay out a series of questions that directors can ask on strategy, risk, financial performance, external reporting, reliability and board structure.

Encourage directors to engage with stakeholders on sustainability priorities. Directors should pursue opportunities to engage with external stakeholders on sustainability priorities to gain different perspectives on issues, rather than being informed exclusively by management. A number of interviewees reiterated that having a multi-stakeholder perspective would help directors make better-informed decisions.

Leading companies are moving in this direction. Directors at *EMC* have attended dialogues with external stakeholders, including investors and advocacy groups focused on the company's sustainability strategy, approach and performance. *Nike's* then-director Jill Kerr Conway, recognizing that labor issues in contract factories would become a significant priority for the company, visited a number of contract factories in Southeast Asia to learn firsthand about labor issues and identify possible solutions. Her knowledge influenced *Nike's* early action to address supply chain concerns in the apparel industry.[39]

"Boards are sometimes isolated. It is important for directors to consider new, unusual and diverse sources of information as they make decisions on sustainability."

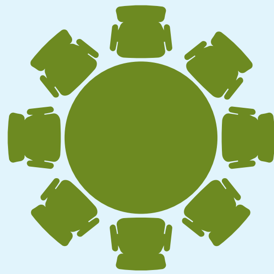
— CERES PROJECT INTERVIEW PARTICIPANT

There is a growing movement to systematize the dialogue between shareholders and directors. The Shareholders-Directors Exchange developed a framework describing the circumstances under which shareholder-director engagement is appropriate and how to make the engagements valuable. Vanguard, one of the world's largest asset managers, proposed the creation of "shareholder liaison committees" in the boards of companies that it invests in.[40] The organization believes this will promote consistent exchanges between shareholders and directors that could help anticipate risks and help boards learn about best practices in other companies. Sustainability issues are a prime example of how this exchange could be used.

Evaluate board performance on sustainability. Most U.S. corporate boards conduct self-evaluations to assess performance, ensure they are discharging their obligations, implement steps for improvement and identify potential gaps in the boardroom.[41] The evaluation is usually conducted by outside legal counsel, most typically through the use of a questionnaire. When sustainability is recognized as relevant to enterprise risk and competitive opportunity, Ceres recommends that the self-evaluation process include an assessment of the board's effectiveness in addressing sustainability priorities.

This is relevant both for companies with explicit board sustainability oversight systems and those without such systems in place. When the board formally considers sustainability, incorporation in evaluations could help build and reinforce oversight mechanisms. When companies do not have formal sustainability oversight in place, evaluations could be an opportunity for introducing these issues into the board agenda.

WHEN SUSTAINABILITY IS RECOGNIZED AS RELEVANT TO ENTERPRISE RISK AND COMPETITIVE OPPORTUNITY, CERES RECOMMENDS THAT THE SELF-EVALUATION PROCESS INCLUDE AN ASSESSMENT OF THE BOARD'S EFFECTIVENESS IN ADDRESSING SUSTAINABILITY PRIORITIES.



COORDINATE BOARD AND MANAGEMENT APPROACHES ON SUSTAINABILITY AND BUSINESS PERFORMANCE

To integrate board sustainability oversight into business operations, companies can:

- **Involve staff with profit and loss responsibility in board discussions on sustainability.**
- **Engage C-Level executives in championing sustainability to the board and across the company.**

While boards are responsible for oversight, management is in charge of strategy development and execution. Management could set the framework for productive and effective conversations on sustainability at the board level by sharing the appropriate information, involving executives from across the enterprise and using the input provided by the board to enhance the organization's approach on key issues. Ceres recommends that corporate boards and senior management work together to ensure that board sustainability oversight aligns with and builds upon management priorities and implementation strategies.

Involve staff with profit and loss responsibility in board discussions on sustainability. In addition to including the corporate staff responsible for sustainability, board discussions of environmental and social priorities should also involve business line leaders accountable for profit and loss. This could include executives with responsibility for finance, risk, product, research and development, and operations. Involving business line leaders would educate both the board and key staff on how sustainability issues impact the company from a functional perspective. The Corporate Secretary, who plays an intermediary role between boards and investors, could also draw the connections between sustainability and financial impacts to both these constituencies.

Nike's Board Corporate Responsibility and Sustainability Committee meetings are staffed by the company's Chief Sustainability Officer and the Chief Operating Officer. Meetings typically include discussions of key sustainability issues as they relate to business functions and progress against those issues. Executives often appear before the committee to discuss how sustainability and business strategies are aligned and how this is reflected in the work of the teams that they lead.

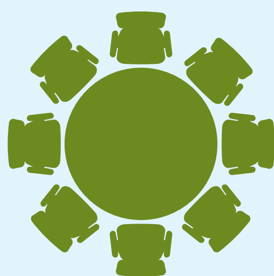
> "Most sustainability executives in an organization are vision setters. However, the board needs to hear not only from the vision setters, but also from the implementers. By doing this, the board will encourage integration and collaboration for sustainability across the organization."
>
> **— BOB FISHER**
> Chairman of the Board, Gap Inc.

Engage C-Level executives in championing sustainability to the board and across the company. Having C-level executives with revenue or risk related responsibilities promote sustainability goals and initiatives will inspire a similar commitment on a board and within a company. Interviewees noted that the CEO, as a member of both the board and management, plays an important role in prioritizing sustainability across the enterprise and to the board. *PepsiCo* Chair and CEO Indra Nooyi's vision for integration led to the development of Performance with Purpose, a strategy that incorporates significant environmental and societal goals with long-term business success.[42] Because of this strategy, *PepsiCo* began expanding its business beyond carbonated beverages and into "better for you" and "good for you" alternatives. As a result, the company's nutrition business comprised 20 percent of net revenue in 2014.[43] The support of *PepsiCo's* board was critical in allowing the company to stay the course on this strategy.

INTEGRATING SUSTAINABILITY INTO BOARD ACTION

The first section of this report outlined strategies that directors and corporate executives could use to integrate sustainability into board systems. To achieve performance impacts, robust systems need to be combined with board action. The following section describes steps that boards collectively and directors individually can take within the context of the systems noted previously and as a part of their governance responsibilities.

The ability of boards to influence performance depends significantly on management and corporate culture. Management and board leaders, such as the CEO and Board Chair, play important roles in ensuring that directors feel empowered to raise critical issues.



EMBED SUSTAINABILITY IN STRATEGIC PLANNING

To make sustainability part of the strategic planning process, boards can:

- **Assess the inclusion of sustainability priorities in business plans.**
- **Champion a long-term mindset.**
- **Evaluate strategic goals to ensure a long-term focus and alignment with sustainability impacts.**
- **Monitor strategy implementation, including sustainability priorities.**
- **Consider sustainability priorities in succession planning.**

While corporate boards do not draft strategic plans, they are responsible for holding management accountable for putting in place a rigorous planning process that includes appropriate timeframes, integration of priorities and strategic goals and monitoring of the implementation of the plan. Directors could consider opportunities to guide sustainability integration as a part of each of these steps.

Assess the inclusion of sustainability priorities in business plans. The board's responsibility for integrating sustainability into the strategic planning process is two-fold. When a sustainability issue is explicitly recognized as an organizational priority, the board is responsible for assessing whether it has been included in the business strategy in a meaningful manner and is being appropriately integrated into the approach of relevant operational companies. When sustainability is *not* explicitly recognized, the board is responsible for considering whether management has conducted assessments that could pinpoint sustainability risks or opportunities, such as including scenario analysis and peer benchmarking.

Some interviewees noted that one way to judge whether board oversight of sustainability is being exercised effectively is to assess the extent of integration between sustainability and the enterprise's core business activities. Companies with mature systems that integrate the two typically have boards that systematically view sustainability through a variety of perspectives, including revenue, risk, reputation and resource implications.

Ford recently renamed its board Sustainability Committee as the "Sustainability and Innovation Committee" to reflect the fact that committee deliberations are increasingly focused on the integration of sustainability into the business strategy and, in particular, the role that technology innovations and partnerships play in meeting key business goals.

Champion a long-term mindset. Another way that boards could embed sustainability issues in corporate strategy is by emphasizing a long-term perspective as a part of the strategic planning process since many sustainability issues become financially relevant in the long-term.

Interviewees noted that corporate leaders and boards are increasingly preoccupied with quarterly earnings targets and do not invest sufficient time in thinking and planning for long-term corporate performance. Indeed, the very notion of what is considered "long-term" has shrunk. McKinsey cites findings that 70- 90 percent of a company's value is related to cash flows that are expected three to five years out.[44] The Audit Committee, which sets the tone for financial reporting, has an important role to play. One approach is to move companies away from the practice of issuing quarterly earnings guidance. A number of corporations, including *Unilever*, *Coca Cola* and *National Grid*, have done just that to encourage investors and stakeholders to focus on longer-term value.[45]

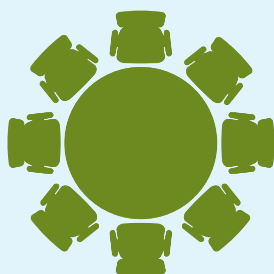
Evaluate strategic goals to ensure they are long term and aligned with sustainability impacts. Boards provide oversight and advice on goals that are set as a part of the strategic planning process. Directors can assess if the strategic goals are long-term and aligned with the company's impacts on sustainability issues. When a sustainability factor is critical to corporate strategy, boards could ask management to consider whether setting specific goals would move the sustainability agenda.

Monitor strategy implementation, including sustainability priorities. When sustainability is explicitly included in business strategy and goals, the role of the board in monitoring implementation and establishing accountability becomes clear. Every year, *American Electric Power's* Board of Directors includes a statement in the company's integrated sustainability and financial report emphasizing that management will be evaluated by its success in executing the company's strategic plan and in being agile in responding to changing circumstances while respecting the commitments in the report.[46]

Consider sustainability priorities in succession planning. One of the primary responsibilities of the board is to put in place a succession plan for the role of the CEO and supervise management's succession planning for other executive officers. When sustainability is identified as a core part of the business strategy, boards should consider knowledge and expertise of sustainability priorities as a part of the core capabilities sought in succession candidates.

"The first job of the board is to ensure that company leadership has the right strategy for long-term, which is robust, agile and resilient. The second job of the board is to ensure that the company has the right leadership team for the long-term –strong leaders, who can be transformative as needed. This should start at the top and go two levels down."

— DAVID STROHM
Venture Partner, Greylock Partners;
Board member of EMC



INTEGRATE SUSTAINABILITY INTO RISK OVERSIGHT

To encourage companies to plan for sustainability challenges, boards can:

- **Request assessments of how sustainability is included in the enterprise risk management process.**
- **Review sector benchmarking and scenario planning.**
- **Raise the importance of key sustainability risks as a part of the strategic planning process.**

Corporate boards are responsible for evaluating how a range of risks – strategic, financial, operational, regulatory, reputational and human resources – could affect the enterprise. Sustainability is a critical part of this dynamic. Boards have an important role to play in systematically considering a company's material sustainability risk exposures and management strategies to mitigate these risks.

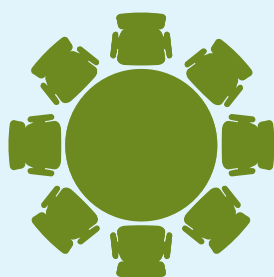
Request assessments of how sustainability is included in the enterprise risk management process. Ceres recommends that board audit committees request assessments of whether and how sustainability practices have been integrated as a part of the Enterprise Risk Management (ERM) process. This could include evaluating processes to identify current and emerging environmental and social risks, crafting plans to mitigate risks, and reviewing the adequacy of resources to address risks and the capacity of the enterprise to respond to unknown risks.

The ERM is a management tool that has a built-in feedback loop, allowing executives and the board to make adjustments if problems are pinpointed.[47] Where relevant, the ERM could include a risk appetite statement with metrics and risk tolerance levels for material sustainability issues.

Review sector benchmarking and scenario planning. Some interviewees noted that overseeing the sustainability risks facing an enterprise requires the recruitment of directors who have relevant industry and sustainability expertise and are able to understand how their company compares with others in the sector on a range of sustainability indicators. Sector benchmarking, which companies

provide to boards to aid this understanding, typically looks at financial, human resource and capital investment, and could be expanded to include environmental and social criteria. Independent external analysis, including scenario planning around key issues, could also help inform the board's role in risk oversight. Ceres' *Road to 2020* and *Gaining Ground* reports provide detailed sector benchmarking and company scorecards on a range of sustainability issues and could be considered helpful resources.

Raise the importance of key sustainability risks as a part of the strategic planning process. When sustainability issues are considered critical to the enterprise, boards should consider their risk exposure in the context of the business strategy. Every six months, UK retailer *Marks & Spencer's* board reviews a group risk profile in which environmental and risks are factored in as contributing to broader risks such as reputation and supply chain. Plan A, the company's integrated sustainability and business strategy, is a summary of the business response to mitigate these risks. The main board is updated on Plan A at least once a year.[48]



INCENTIVIZE MANAGEMENT

To motivate management to drive sustainability performance, boards can:

- **Link compensation to sustainability.**
- **Implement long-term performance incentives.**

Boards are responsible for aligning management incentives with the strategic plan for the business and rewarding the right behavior. Building on their roles in strategic planning and risk oversight, Ceres recommends that boards incorporate environmental and social priorities into their process for evaluating and compensating management performance.

Link compensation to sustainability. The link between compensation and sustainability is a growing area of investor focus. Between 2011 and 2015, Ceres tracked over 25 shareholder resolutions calling on board compensation committees to tie executive pay to relevant sustainability metrics. In spite of growing investor attention, the number of large companies linking executive compensation to sustainability priorities remains small. The Gaining Ground report identified that only 24 percent of large US companies assessed linked executive compensation to sustainability priorities in a meaningful manner.[49]

Where sustainability is tied to executive compensation, the board typically prioritizes the most material sustainability issues for the enterprise. Leading companies ensure that sustainability factors prioritized in this way form a meaningful part of overall remuneration. For example, given the continuing relevance of safety to the utility industry and as a part of its efforts to strengthen safety performance, *PG&E's* board linked 50 percent of management's at-risk performance-based pay to the company's workforce and public safety performance, and provided details of the weights assigned in their annual proxy filing.[50] Another approach is to tie executive compensation to a basket of indicators reflecting a range of corporate priorities, including sustainability. Some companies, including *BHP Billiton* and *Campbell Soup*, use a "balanced scorecard" that incorporates business and sustainability priorities into a suite of indicators used to determine short- and long-term performance payouts. This helps to ensure that both sustainability and financial goals are prioritized.[51]

BOX 7: INTEGRATING SUSTAINABILITY INTO COMPENSATION

In its report ***Integrating ESG issues into Executive Pay***, the UN PRI recommended that companies integrate sustainability into compensation structures as follows:

- Adopt a clear process for identifying sustainability metrics that relate to shareholder returns and corporate strategy.
- Link sustainability metrics to reward systems as a meaningful part of the overall remuneration framework.
- Disclose the rationale, method and challenges presented by the integration of sustainability metrics into executive pay.

Implement long-term performance incentives. Compensation is another way that boards orient management towards thinking and planning for performance in the short and long terms. Some interviewees noted that current compensation systems are overwhelmingly weighted towards short-term performance and that investors are often caught up in the same mindset. The Aspen Institute's *Guiding Principles for Long-Term Value Creation*[52] lays out a set of principles by which board Compensation Committees can incorporate long-termism across all performance-based compensation systems, including annual bonuses and retirement plans. The Principles note that compensation should support long-term value creation, as well as the long-term, sustainable growth of the enterprise.

DISCLOSING THE ROLE THE BOARD PLAYS

Companies should provide more disclosure on how the board oversees sustainability, including priorities set and decisions made.

The previous sections discussed a number of strategies for integrating sustainability into governance systems and board action in order to allow for effective board sustainability oversight. However, without disclosure on the role of boards in sustainability, investors and other stakeholders cannot gauge where this oversight is being exercised effectively, including when the accountability systems in question are influencing performance change.

There is a growing call for companies to disclose not only more information, but also more relevant information on their material sustainability plans and performance in their financial and sustainability disclosures. This demand for transparency requires that companies evolve how they disclose board oversight as well. Currently, most companies provide very limited information on how board oversight is exercised on any specific issue, including sustainability. Disclosure is typically in the form of a high-level description of board oversight systems and does not include details that would allow stakeholders to assess whether the oversight is being implemented in a robust manner. While acknowledging the concern that expanding disclosures could have the potential of exposing companies to increased liability risks, Ceres contends that there are ways for companies to be more transparent about the specific material sustainability issues that the board discusses and key decisions made, without invoking such liability.

As a first step, disclosures should include narrative on the board's assessment of the company's material sustainability priorities and how these are being integrated into the business plans and performance. Many companies' sustainability reports include messages from the CEO and the Board Chair, which could be a great forum for this discussion. Such disclosures could also be provided in the annual or proxy reports. Building on this, companies could disclose the impact of board oversight on the priorities identified, including focus areas and key decisions made, such as those that affect planning, risk oversight and incentives. For instance, *Apache's* 2014 Sustainability Report notes that the Board met with almost 60 percent of the company's shareholder base, and notes the changes that followed to its compensation and governance provisions.[53] While this example highlights a shareholder focus area, this could be replicated in the case of broader sustainability issues. Finally, disclosures could incorporate details on the elements of board sustainability oversight as noted in this report. More transparency on the board's process for guiding sustainability could motivate companies to establish clear systems, while also driving these systems towards performance results.

Investors and other stakeholders have a corresponding responsibility to ask questions relating to how board sustainability oversight is being exercised and to seek more disclosure.

CONCLUSION

Sustainability issues pose significant risks and opportunities for value creation across all industry sectors. Those companies that can systematically identify and assess current and emerging sustainability impacts will be better able to adapt, mitigate risks and compete in a 21st century economy. Decisions on how best to address sustainability issues must be made at the highest levels of the enterprise, including at the board level.

This report provides a number of options for companies to consider as they think through what effective board sustainability oversight could mean for their enterprise. There is no single solution to the question of how boards should oversee sustainability. Boards and senior management must determine what works best for their company and the evolving circumstances of the enterprise. Engaging with stakeholders as a part of this will help companies proactively identify and understand sustainability practices that will bring long-term value to shareholders and stakeholders.

Ceres' *Gaining Ground* report notes that while we are seeing some corporate progress on sustainability performance, we are simply not seeing change at the pace and scale that we need. Creating robust links between governance systems, such as board sustainability oversight on one hand and performance impacts on the other will catalyze the on-the-ground changes that Ceres and our partners are working towards. However, in addition to strengthening governance systems, there is also an important need to increase the number of companies that are willing to engage on these issues. Directors, senior corporate leaders and other stakeholders have critical roles to play in moving this agenda forward.

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