



Shareholder Association
for Research and Education

**Submission to the
National Roundtables on Corporate Social Responsibility**

Submitted by the
Shareholder Association for Research and Education (“SHARE”)

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Introduction

The Shareholder Association for Research and Education (“SHARE”) is a national non-profit organization dedicated to assisting institutional investors in their consideration of the long-term social, environmental and economic impacts of their investment decisions. SHARE was created in 2000 by the Canadian labour movement to provide leadership on responsible investment activities at both a national and international level.

SHARE appreciates the opportunity to submit comments to the Canadian Government as a part of the public consultations of the National Roundtables on Corporate Social Responsibility. The Roundtable process is an important exercise in multi-stakeholder dialogue and debate, and it addresses issues facing the extractive industry that are important to Canadian investors. The outcome of the Roundtables has the potential to affect company and investor behaviour, and creates an opportunity for the Government of Canada to take significant and meaningful steps to address the concerns raised by civil society, labour unions, investors, industry and indigenous groups regarding the conduct of Canadian extractive companies overseas.

Below, SHARE describes three reasons why action by the federal government is both necessary and desirable: Canadian investor’s significant exposure to the extractive sector, the increasing significance of international legal and voluntary standards and norms, and the potential to create a win-win situation through improved capital market disclosure, financial analysis and investment decision-making. Our submission identifies recommendations that fall into two broad areas. First, an opening exists for the federal government to play a role in clarifying and articulating standards and expectations for Canadian corporations and investors based on international laws and norms. In particular, attention is drawn to the importance of supporting and promoting the expectation that companies and investors will respect the Universal Declaration of Human Rights and the International Labour Organization’s Core Conventions. Second, the federal government and the Canadian Securities Administrators have an opportunity to encourage responsible capital market behaviour and improve corporate social and environmental performance by strengthening the disclosure and transparency requirements for companies and their investors.

Rationale for Federal Government Action

Investor exposure to the extractive sector

Energy and materials companies comprise approximately 43% of the S&P/TSX Composite Index. As a result, mining and oil and gas companies are highly represented in the investment portfolios of institutional investors and significantly influence the financial risks, returns and opportunities they face.

Publicly traded extractive companies that engage in risky activities in overseas markets where legal and regulatory structures are not well developed, or where significant economic, social and environmental impacts have the potential to derail production, ultimately pass those risks on to their shareholders.

Relevance of foreign and international standards

Global economic integration and interdependency has created conditions whereby Canadian companies are increasingly subject to overseas regulations or international expectations and standards. For example, legal action has been brought against Canadian corporations with operations in the United States under the Alien Tort Claims Act (ATCA), which potentially can have a significant influence on their operations and financial liabilities. Similarly, in the electronics industry, European Union regulations to control the use of certain hazardous chemicals under the RoHS directive¹ place restrictions on Canadian companies producing and selling electronics equipment in the European market.

In addition to the impact of environmental and social laws and regulations, a robust and sophisticated network of codes, standards and best practices under development at the global level is creating greater expectations and setting higher standards for companies operating internationally. For example, the United Nations Global Compact, the OECD Guidelines for Multinational Enterprises (“the OECD Guidelines”), the Equator Principles and the Voluntary Principles on Security and Human Rights (“the Voluntary Principles”) outline key principles of responsible business conduct that stakeholders are increasingly using to identify and define acceptable and unacceptable corporate practice. Codes, standards and best practices to which many large Canadian companies voluntarily adhere, are a product of this evolving international dialogue and the ability of Canadian extractive companies to attract international investors will be enhanced by aligning Canada’s domestic approach to corporate responsibility with these prominent international initiatives.

The OECD Guidelines for Multinational Enterprises is one such standard that has the potential to effectively guide and promote responsible corporate conduct in Canada. While certain reforms are required to make the mechanisms of the Guidelines more accessible and effective, they stand out as the best framework for establishing a national strategy for corporate responsibility, particularly because they were created by an organization of national governments and they embody and uphold international principles, standards and norms. The Guidelines also have an accountability mechanism, a feature that is absent in many voluntary standards. In countries where national governments have supported multi-stakeholder participation in the National Contact Point (“NCP”) such as in Belgium, Denmark, Sweden, France, and Norway, this mechanism has been quite successful.

Some extractive sector companies recognize that international standards-setting and domestic regulation go hand in hand, and they have responded positively to stakeholders’ attempts to increase corporate transparency and accountability. Other companies, however, lag behind and continue to operate with little regard to evolving international norms. Paul Mitchell, the Secretary General of the International Council on Mining and Metals (“ICMM”) has stated that for large global mining companies, a commitment to promote sustainable development makes good business sense because it is the best way to protect brand reputation and mitigate risks.² Mr. Mitchell has called for more government action to address the market imbalances that allow

¹ Stands for the restriction on the use of certain hazardous substances in electrical and electronic equipment. See <http://www.rohs.gov.uk/> for more information.

² Paul Mitchell, *Maintaining Market Access for Metals - a Shared Responsibility* (April 7, 2006 [cited August 20, 2006]); available from www.icmm.com/news/1269Intergalva-PaulMitchell.pdf.

laggards to continue to operate unabated arguing, “Governments need to regulate more, and companies have to be more cautious [about] where they put their money.”³ The Canadian Government has a clear role to play in levelling the playing field for industry leaders and providing direction and assistance for industry laggards.

Recommendation 1: Renew the federal government’s commitment to the OECD Guidelines for Multinational Enterprises and Canada’s National Contact Point (NCP) and strengthen the NCP’s mandate, powers and resources by:

- a) Creating a tripartite structure for Canada’s National Contact Point and creating a mechanism through which the NCP can formally and regularly consult with experts from other municipal, regional or national governments, unions, business leaders, investors, academia and civil society organizations;
- b) Granting the NCP the power to investigate claims and conduct fact-finding missions;
- c) Ensuring that the NCP is prepared to accept complaints that meet the Guidelines’ procedural requirements irrespective of the existence or non-existence of parallel legal proceedings;⁴
- d) Where the parties do not reach an agreement, enabling the NCP to issue a public statement outlining the results of the case, as required by the OECD Guidelines, and to provide recommendations to such parties on how to achieve compliance with the Guidelines;⁵ and
- e) Expanding promotional and educational programs and tools for companies, civil society organizations and relevant government bodies regarding the services provided by Canada’s NCP.

The Canadian Government can help minimize the risks and uncertainties for companies and their investors by clearly articulating the standards and guidelines by which Canadian corporations are expected to follow when operating overseas. This is especially important in countries where political and regulatory uncertainties may influence the ultimate success or failure of a project. For example in Esquel, Argentina local protests and political opposition succeeded in stopping the construction of a gold mine under development by Canadian company Meridian Gold, resulting in lost revenue for the company and its investors. In contested, unstable or volatile regions where governance is weak, clear expectations and tools for managing social and environmental concerns can go a long way in helping companies identify and address issues that may have environmental or social consequences, before they create costly or dangerous conflicts.

Recommendation 2: Clarify the Government of Canada’s expectations for responsible business conduct and encourage Canadian companies to adopt and implement established international standards and codes of practice by:

- a) Becoming a signatory to the Voluntary Principles and asking Canadian companies that employ public or private security at their operations overseas to do the same;⁶

³ James Langman, "Socially Responsible Gold Mining Urged," *The Washington Times*, August 15, 2006.

⁴ Trade Union Advisory Committee to the OECD (TUAC), "Specific Instance and Parallel Proceedings - Draft Summary of Discussions [Daf/Inv/Wp/Wd(2005)1/Rev2]," (Paris: May 15, 2006).

⁵ Ibid.

⁶ In its response to the SCFAIT report the Government stated it was considering becoming a signatory of the Voluntary Principles.

- b) Developing education programs and tools to publicize and disseminate information on the OECD Guidelines, the Voluntary Principles, corporate social responsibility and relevant international laws, standards and best practices; and
- c) Harmonizing efforts to promote these initiatives across all departments of the Government of Canada.

Recommendation 3: Provide specific guidance to companies operating in weak governance zones (especially in intra-state conflicts) on the expectations of business conduct, particularly where human rights violations are clearly documented, by:

- a) Requiring companies operating in weak governance zones that apply for Export Development Canada, Trade Commissioner Service or Canadian Embassy financial or promotional support to review the OECD’s “Risk Awareness Tool for Multinational Enterprises in Weak Governance Zones.” Make such support conditional on companies issuing annual public reports on the operational risks and risk mitigation strategies and practices employed in these regions; and
- b) Publishing a checklist of government-recommended “relevant international instruments,” as outlined in the “Risk Awareness Tool for Multinational Enterprises in Weak Governance Zones.” The checklist should include: the Universal Declaration of Human Rights, the ILO Core Conventions, the ILO Tripartite Declaration, the OECD Guidelines, the Voluntary Principles and the Extractive Industry Transparency Initiative.

Facilitating market action

Investors and asset managers are paying increasing attention to how social, environmental and governance (“ESG”) risks and opportunities affect the value of their investment portfolios. A number of high profile investors in Canada have made commitments to consider ESG issues in the selection and management of their investments. For example, the Canada Pension Plan Investment Board (“CPPIB”) and the Caisse de dépôt et placement du Québec (“CDP”) recently adopted Responsible Investing policies, and the CPPIB, CDP and the British Columbia Investment Management Corporation have signed the United Nations Principles for Responsible Investment (“UN PRI”).⁷

Large, long-term investors, such as pension funds, can play a unique role in facilitating change, provided that the appropriate policy framework is in place to integrate ESG factors into corporate analysis and investment decision-making. Several OECD governments have taken the approach of strengthening the accountability of institutional investors to unit holders and beneficiaries. This is an effective way to create an incentive for companies, prompting them to operate responsibly and mitigate social and environmental impacts in an effort to attract more investment from large institutional investors.

However, adoption of Responsible Investment policies by institutional investors in Canada has lagged behind other countries, particularly because the common interpretation of fiduciary duty has discouraged fiduciaries from considering ESG factors. While the emerging international

⁷ The UN Principles for Responsible Investment are a set of voluntary principles that promote active ownership practices and the integration of social, environmental and governance issues into investment decision-making (www.unpri.org). Asset owners and investment managers representing approximately \$5 trillion have endorsed the UN PRI.

consensus recognizes that the law does not prohibit trustees from considering social & environmental factors in their investment decision-making,⁸ confusion on this matter persists. The absence of clear direction from relevant government bodies explicitly stating that the consideration of social & environmental issues for the purpose of risk minimization and/or long-term value maximization is not in conflict with established fiduciary duties has been a major factor limiting the consideration of ESG issues in the Canadian investment industry.⁹ To remedy this problem, several OECD jurisdictions including Australia, Germany, France and the United Kingdom, have adopted regulations requiring pension funds and certain other institutional investors to add new disclosure requirements for fiduciaries that make explicit the duty to consider these factors.

Recommendation 4: Increase the social and environmental disclosure requirements for federally governed pension funds by:

- a) Amending the *Pension Benefits Standards Regulations, 1985* to require federally registered pension funds to disclose the extent (if at all) to which ESG considerations are taken into account in proxy voting activities, and the selection, retention and management of investments; and require pension funds to annually disclose their proxy voting guidelines and voting records; and
- b) Amending section 48 (annual report) of the *Public Service Pension Investment Board Act, 1999* and section 9 (statement of investment policies, standards and procedures) of the *Public Service Pension Investment Board Regulations, 1999* to implement the recommendation in 4a) above.¹⁰

Despite perceived restrictions imposed by the traditional interpretation of fiduciary duty, institutional investors have continued to raise the profile of social and environmental issues in recent years by filing shareholder resolutions and voting their proxies. The number of shareholder proposals filed by investors that address social and/or environmental impacts of Canadian companies has increased markedly, as has general investor support for them. In 2004 7.4% of shareholder resolutions submitted to Canadian companies referred to social and/or environmental issues; by 2006 that number increased to 26.8%.¹¹ Substantial shareholder support for resolutions filed with Alcan, Bombardier, Nortel and Power Corporation regarding

⁸ See Freshfields Bruckhaus Deringer, "A legal framework for the integration of environmental, social and governance issues into institutional investment," Produced for the Asset Management Working Group of the UNEP Finance Initiative, October 2005; Yaron, Gil, "Fiduciary Duties, Investment Screening and Economically Targeted Investing: A Flexible Approach for Changing Times," Shareholder Association for Research and Education (SHARE), www.pensionsatwork.ca/english/project_pages/project_5.php (accessed September 11, 2006); S. Prakash Sethi, "Investing in Socially Responsible Companies is a Must for Public Pension Funds – Because there is no Alternative," *Journal of Business Ethics* 56 (2005): 99-129.

⁹ Wheeler, David, Jane Thomson, Therese Woodward and Priti Shokeen, "Comparative Study of UK and Canadian Pension Fund Transparency Practices" Schulich School of Business & York Institute for Research in Innovation and Sustainability with Kingston Business School, May 2004.

¹⁰ This action item is partially fulfilled by the disclosure of the PSPIB's Social and Environmental Responsibility Policy, available on its website, however this action item would additionally require *annual* disclosure of the PSPIB's consideration of ESG issues regarding the ongoing management of investments, and annual disclosure of its proxy voting record.

¹¹ The statistics are based on an analysis of SHARE's Shareholder Resolutions Database, available online at <http://www.share.ca/en/shareholderdb>. Data for 2006 is for the period of January 1 to November 1, 2006.

human rights, are notable, and demonstrate that investors have a strong interest in monitoring the environmental and social performance of Canadian companies.

Investment analysts now increasingly recognize that ESG policies and performance can have an impact on reputation, liability, customer loyalty, operational efficiency, and ultimately on financial performance, and they are starting integrating these factors into financial valuations. The Enhanced Analytics Initiative (see www.enhancedanalytics.com)¹² was formed to support and fund high quality research that systematically analyzes the impact of ESG factors on long-term financial performance and investment returns. A notable example of this research is an extensive report on the mining sector written by Citigroup. The report effectively demonstrates how analysts can link valuations of mining companies to their social, political and environmental risk exposure. Researchers identified additional risks and opportunities that analysts had not previously considered, and the analysts were able to adjust buy/sell ratings to reflect each company's ability to manage these risks.¹³

Recommendation 5: Support and encourage the consideration of social and environmental factors in mainstream financial analysis and provide guidance to help Canadian investors more carefully consider the impact of these factors on corporate performance and long-term investment risks and opportunities by:

- a) Endorsing and promoting the United Nations Principles for Responsible Investment as a preferred framework for guiding Canadian investor behaviour;
- b) Developing and disseminating materials to educate institutional investors, investment service firms and fund managers on the UN PRI;
- c) Ensuring that, where Government of Canada funds are invested in public markets, they are invested in accordance with the UN PRI.¹⁴

Just as financial analysts rely on transparent and timely disclosure of financial information, high quality ESG analysis requires credible and comparable reports that provide detailed information on environmental and social performance. In order to meet this need, the Global Reporting Initiative ("GRI") (see www.globalreporting.org) has developed reporting guidelines that help companies prepare reliable Sustainability reports. The GRI has created a robust system that supports the work of international bodies such as the United Nations Environment Program, and it has recently formed a partnership with the UN Global Compact to encourage Global Compact signatories to standardize their reporting practices. Limitations posed by variable standards and requirements in different industries and sectors have been overcome by the creation of technical protocols and sector supplements, such as the mining sector supplement, which was developed in cooperation with the ICMM. The Canadian Government can play a key role in developing GRI guidance materials for the oil & gas industry and providing support for junior mining and oil & gas companies that agree to prepare GRI reports.

¹² The participants in the Initiative, which collectively manage \$1 trillion in assets, have pledged to contribute 5% of their brokerage commissions to fund research that considers ESG factors in mainstream financial valuations.

¹³ Heath Jansen, Mike Tyrrell, and Alan Heap, "Towards Sustainable Mining: Riding with the Cowboys, or Hanging with the Sheriff?," (Citigroup Global Portfolio Strategist, March 14, 2006).

¹⁴ The Principles outlined in the UN PRI are consistent with the PSPIB's own Social and Environmental Responsibility Policy, dated February 3, 2005 (available online at http://www.investpsp.ca/en/frame_set.htm).

Recommendation 6: Support the work of the Global Reporting Initiative by:

- a) Providing financial support to the GRI and assist in the creation of GRI technical protocols and sector supplements for the oil and gas industry; and
- b) Helping the GRI create reporting guidance that is relevant to, and useful for, junior mining and oil and gas companies.

While SHARE believes government-led initiatives, such as the ones outlined above, should formulate the government's agenda for change, we recognize that key actions by other national decision-making bodies are also necessary to achieve the desired outcomes. As a result, we provide the following recommendations to the Canadian Securities Administrators ("CSA") and we encourage the federal government to follow up with the CSA in a timely manner to ensure that appropriate steps are taken in a manner consistent with the Canadian Government's objectives.

Recommendation 7: To the Canadian Securities Administrators

- a) Clarify for investors, companies and other stakeholders the definition of "materiality" in regards to social and environmental factors. Make a public statement specifying that social and environmental issues that have the potential to impact company performance, reputation, liability and value constitute material information requiring timely and transparent disclosure.
- b) Create a National Instrument that requires extractive sector companies to: i) report known material ESG risks & liabilities in financial statements; ii) report forward-looking information on potential material ESG risks & risk mitigation strategies in the MD&A;¹⁵ and iii) disclose the extent to which corporate policies and procedures comply with the OECD Guidelines (see Recommendation 1 above). Companies should indicate if, and in what way, corporate policies and the OECD Guidelines diverge.
- c) Encourage companies to disclose important ESG information that may not be material, but that may be relevant to shareholders and other external stakeholders in separate corporate social responsibility (CSR) or sustainability reports. Recommend that companies utilize the tools and reporting guidelines of the Global Reporting Initiative to ensure these reports are transparent, credible and comparable. Make these reports publicly available on SEDAR or other future document repositories.

¹⁵Gil Yaron, "Corporate Disclosure of Material Social and Environmental Information," (Shareholder Association for Research and Education (SHARE): Memo to the Ontario Securities Commission, 2005). **NOTE:** National Instrument 43-101 governs how extractive companies disclose scientific and technical information about mineral projects and outlines the requirements for preparing technical reports. This national instrument requires companies to discuss and disclose "legal, environmental, political or other issues and factors" that are relevant to the technical report and that may materially affect the estimate of mineral resources and mineral reserves. Changes to disclosure requirements or materiality definitions in NI 43-101 would not create change that would result in meaningful disclosure of ESG issues to investors, primarily because the instrument applies exclusively to technical reports and refers mainly to the impact that ESG factors have on mineral reserve estimates. The instrument fails to consider the impact of ESG issues on other factors such as reputation and legal liability that may have a material impact on company performance. Furthermore, because investors base their investment decisions primarily on the information provided in the financial statements and MD&A, and not on technical reports, we believe annual filings (and not technical reports) are the best documents in which to ask for greater disclosure of material ESG risks and liabilities.

Conclusion

The Canadian Government has a central role to play in addressing the concerns raised by investors, community groups, NGOs, unions and academics regarding the social and environmental impacts of Canadian corporations overseas. The most pressing issues identified here stem from a lack of clear expectations for Canadian corporations operating overseas, and the need for more stringent disclosure standards.

Greater disclosure on the part of both investors and corporations will facilitate the creation of market mechanisms that reward industry leaders who take an innovative approach to sustainable and responsible business. Increased transparency requirements for investors will also encourage industry laggards to adopt better practices as a strategy for attracting investment. Finally, vague or inconsistent rules, guidelines and expectations create uncertainties for companies and increase risks for investors. Therefore, government action that articulates clear expectations based on internationally developed and recognized tools, standards and best practices will improve corporate accountability and transparency, decrease the risks faced by Canadian shareholders and create new opportunities for investment.

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For more information about this report, please contact:

Ashley Hamilton
Shareholder Association for Research and Education (SHARE)
1200, 1166 Alberni Street
Vancouver, British Columbia
Canada V6E 3Z3
(604) 408-2456
ahamilton@share.ca