



## **ESG WORKING GROUP**

**Advice to the Eumedion Board on the mission of  
Eumedion**

## TABLE OF CONTENTS

	<b>Page</b>	
<b>Section 1</b>	<b>Preface and executive summary</b>	<b>3</b>
<b>Section 2</b>	<b>Should investors play a role in ES issues</b>	<b>5</b>
<b>Section 3</b>	<b>Eumedion and ES</b>	<b>15</b>
<b>Section 4</b>	<b>Practical consequences for the internal Eumedion procedures</b>	<b>22</b>
<b>Section 5</b>	<b>Recommendations of the working group</b>	<b>23</b>
<b>Annex</b>	<b>Members of the working group</b>	<b>24</b>

## 1. Preface and executive summary

Environmental and social issues are fast becoming more than just buzz words. Customers, communities, business partners, investors, governments, non-governmental organizations and others are increasingly asking companies to explain what it is they are doing to address their environmental and social (ES) impacts. Also institutional investors are increasingly faced with this question. The size of their shareholdings means that major institutional investors have the potential to exert considerable influence on (the decision-making process in annual general meetings of shareholders of) companies in which they invest. In addition, institutional investors are expected by stakeholders to make use of their shareholders' rights in order to make improvements. In the Dutch context, this increased attention and awareness of ES issues has led to the design of principles and best practice provisions, which have been included in the Dutch corporate governance code. The aim of these is to improve the management of ES issues by Dutch listed companies. Against this background and also in reaction to questions by (potential) participants of Eumedion, the General Board of Eumedion has decided to establish a working group to explore the question of whether and how the mission of Eumedion should be broadened to address ES issues.

This working group consisted of 8 members that represent different kinds of participants of Eumedion. The working group members have met 5 times to discuss this question. The working group established 2 sub groups to draft this report. The main findings of this working group as well as its recommendation to the General Board of Eumedion are:

- A growing body of evidence suggests that ES issues are financially relevant to companies and therefore closely linked to investors' interests. There is increasing investor activity on these issues both within individual countries and through international networks. Collaborative investor initiatives have the potential to be an efficient way of pooling resources and maximising effectiveness in monitoring, analysing and influencing companies. As such there is a strong case for institutional investors in the Netherlands to collaborate on ES issues, also within the Netherlands. Engagement on ES issues can serve investors' interests, in relation both to companies that are already well-advanced in their management of ES issues in order to maintain their position, and to those that are less highly advanced and may face financial risk and public scrutiny of their performance in order to improve their performance.
- There is a case for addressing the ES issues within the organisation of Eumedion. There are several arguments in favour of the extension of the mission of Eumedion. The most important arguments are i) cooperation on ES issues between institutional investors will contribute to maintaining their licence to operate, (ii) the Dutch corporate governance code contains principles and best practice provisions regarding ES issues and it is expected by stakeholders that major shareholders, in particular institutional investors, use their shareholders rights in order to encourage listed companies to take actions to address ES issues, and (iii) one integrated platform for ES and corporate governance is preferable above more platforms. Due to its reputation,

acceptance and strengths Eumedion seems to be the natural integrated platform for institutional investors.

- Eumedion is currently strongly associated with corporate governance. It is important to take into consideration that this strong reputation could be lost if Eumedion broadens its mission to ES issues unconditionally, because of the wide and complex nature of ES issues. Therefore, the corporate governance framework should remain the starting point for Eumedion to address ES issues. Eumedion should broaden its mission to ES issues that fall within Eumedion's current corporate governance framework, which for now means focusing on risk management, disclosure and remuneration policy related to ES issues relevant to shareholders. The cooperation on ES issues should be given form at collective level and at an individual level. At collective level, participants of Eumedion should cooperate by reactive involvement in policy making and policy engagement on ES issues only in the Dutch context. At an individual level, the cooperation should be given form by cooperation with regard to the company (general meeting of shareholders), as currently is being done with regard to the general meeting of shareholders on corporate governance issues.
- Future developments may lead to evolved or changed opinions of participants of Eumedion. In order to take these into account the activities and developments around the broadening of Eumedion's mission to ES issues should be at the end of 2010. When evaluating Eumedion's position, further developments or improvements could be considered.

**RECOMMENDATIONS: Having considered the aforementioned arguments, the working group advises the General Board of Eumedion to broaden the mission of Eumedion to risk management, disclosure and remuneration policy related to ES issues that are relevant to shareholders. The working group recommends that the new mission be integrated into the existing Eumedion committees and that the Charters of these committees be amended. The working group finally recommends employing one experienced staff member with specific ES expertise.**

## 2. Should investors play a role in ES issues?

### 2.1 A definition of ES issues

Sustainable business and corporate social responsibility are all phrases that address wider ES issues of doing business. A large number of investors are working actively on ES issues through the UN-sponsored Principles for Responsible Investment<sup>1</sup> - a network of ca. 480 investors with over \$18 trillion USD AUM in total assets under management<sup>2</sup>. But what are these issues? In defining this, the Burgmans Committee refers to the report of the SER<sup>3</sup> (Social and Economic Council of the Netherlands) titled "De winst van waarden" (2000). The SER identified two elements which are of relevance for corporate social responsibility and as such for ES issues:

- 1) Consciously targeting business activities at value creation in three dimensions - Profit, People, Planet - and hence at contributing to society's prosperity in the longer term;
- 2) Maintaining a relationship with the various stakeholders which is based on transparency and dialogue and which responds to legitimate demands from society.

With this in mind, this report defines ES issues as:

*All relevant ES risks and opportunities affecting companies from an investors' perspective. These apply to all companies (Dutch or foreign companies, listed or not) and may relate to company specific issues (e.g. human rights issues at a company) as well as sectoral issues (e.g. pollution standards for automobiles industry) or global issues (e.g. Global Compact standards).*

#### *Are ES issues significant?*

In order to assess whether there is a role for Eumedion in relation to the management of ES issues by Dutch companies, it is important to assess the significance of these issues for investors and their beneficiaries in a general sense. This can be considered from the perspective of both financial relevance and social responsibility. In recent years it has become increasingly clear that the way companies manage a wide range of ES issues can affect their financial performance. Recent research suggests a link between ES issues and the financial performance of investment portfolios.<sup>4</sup>

This can be driven by factors including changing regulation that imposes new requirements and costs on businesses; trends in customer preferences and tastes; society's expectations relating to ethical standards in business; or trends in commodity or labour markets (e.g. energy prices or skill shortages). Taking these factors seriously may have positive effect; not taking them into account the opposite. Different issues are important in different sectors. However, examples of significant issues include:

- **Climate change**

The effects of climate change are now being felt widely across many sectors. The EU's policy

---

<sup>1</sup> [www.unpri.org](http://www.unpri.org)

<sup>2</sup> As of April 2008.

<sup>3</sup> The SER is a government advisory body on social and economic issues.

<sup>4</sup> See for example *Demystifying Responsible Investment Performance*, UNEP Finance Initiative, [http://www.unepfi.org/fileadmin/documents/Demystifying\\_Responsible\\_Investment\\_Performance\\_01.pdf](http://www.unepfi.org/fileadmin/documents/Demystifying_Responsible_Investment_Performance_01.pdf)

response to climate change has created a price for carbon that is clearly visible to industries included in the Emissions Trading Scheme that are now required to pay for the right to emit carbon dioxide above a specified cap. Climate change has thus led to a direct cost to companies, and this can also be reflected in investors' and analysts' assessments of companies' performance and prospects. The extent to which companies are able to reduce their carbon dioxide emissions – by cutting energy consumption or reconfiguring their business – is a factor in their competitive positioning, and thus directly relevant to investors. The physical impacts of climate change, too, are being felt in certain sectors. An increase in the value of storm-related claims is being seen in the insurance industry, and natural resource extraction companies are reviewing their global operations to understand their exposure to damage from extreme weather events. Companies' degree of understanding of these issues and their capability to deal with them are directly relevant to their business performance, and thus to investors.

- **Supply chains, including child labour**

Companies' ability to manage their supply chains in accordance with internationally recognised standards such as those of the International Labour Organisation can be a significant factor in winning and retaining the trust of their customers. Allegations of child labour or other supply chain malpractice can seriously damage a company's reputation, with adverse business implications. The local context in which many emerging markets companies are operating plays a relevant role which multinationals need to balance with internationally recognised standards.

- **Environment and social impacts on local communities**

Companies in the oil and mining industries in particular are under intense public scrutiny over their relations with local communities. This is particularly true in the developing world, where regulation of these issues, or governments' ability or willingness to enforce it, may be weak. In such cases the management of these issues can affect operations that are material – in the accounting sense – sources of revenue for the companies concerned. Disruption of these operations as a result of failure to manage ES issues sensitively would have direct and large-scale impacts on share prices.

- **Business ethics**

Probity and honesty in business dealings are a matter not just of ethics but of direct relevance to the bottom line. Bribery and corruption can lead not only to criminal prosecution, but also to financial penalties and loss of business that are highly material to shareholders. Siemens, UBS, Parmalat, Enron and Worldcom are among recent examples of companies that have suffered large-scale (in some cases terminal!) financial damage as a result of business ethics failures.

#### *Specifically Dutch dimensions to ES issues*

Certain ES issues are particularly relevant in the Dutch context because there is a high level of government, NGO or general public interest in them. These include, but are not limited to:

- Climate change and upcoming CO<sub>2</sub> regulation: In particular because the Dutch government has expressed a strong position with regard to maintaining climate change goals despite the economic crisis.
- Sustainable building: In the Netherlands there is limited space and a high need for work and living accommodation. Energy efficiency in buildings has strong links both to sustainability (via CO<sub>2</sub> emissions) and to financial performance (via occupiers' demand for low energy costs).
- Child labour: Dutch government has proclaimed taking the lead within the EU with regard to combating child labour in the supply chain.
- Transparency with regard to supply chain: Legislation to provide consumers with supply chain information to enable to make informed choices is under development.
- Most Dutch companies are very internationally oriented. Global operations are particularly sensitive to ES risks, given that legislation on these issues may be weak in some markets, legislation that does exist is often poorly enforced, and stakeholders in the Netherlands and other developed countries are strongly focused on issues in emerging markets.

#### *Corporate governance and ES issues*

To the extent that ES issues are relevant and significant factors for a company's business, it is important that the board (and other aspects of the governance structure) contribute to ensuring that the issues are appropriately managed. The composition of management and supervisory boards needs to reflect the appropriate skills and expertise, and internal control and risk management systems and procedures need to be appropriately designed and overseen.

The new Dutch corporate governance code now explicitly mentions corporate social responsibility in its preamble<sup>5</sup>, principle III.1<sup>6</sup> and best practice provision III.1.6<sup>7</sup> and, most important, principle II.1<sup>8</sup>, which stipulates:

*"The role of the management board is to manage the company, which means, among other things, that it is responsible for achieving the company's aims, the strategy and associated risk profile, the development of results and corporate social responsibility issues that are relevant to the enterprise. The management board is accountable for this to the supervisory board and to the general meeting. In discharging its role, the management board shall be guided by the interests of the company and its affiliated enterprise, taking into consideration the interests of the company's stakeholders. The management board shall provide the supervisory board in good time with all information necessary for the exercise of the duties of the supervisory board."*

<sup>5</sup> Which stipulates under point 8 "The management board and the supervisory board should take account of the interests of the various stakeholders, including corporate social responsibility issues that are relevant to the enterprise".

<sup>6</sup> The supervisory board shall also have due regard for corporate social responsibility issues that are relevant to the enterprise.

<sup>7</sup> Which stipulates that the supervision of the management board by the supervisory board shall include corporate social responsibility issues that are relevant to the enterprise.

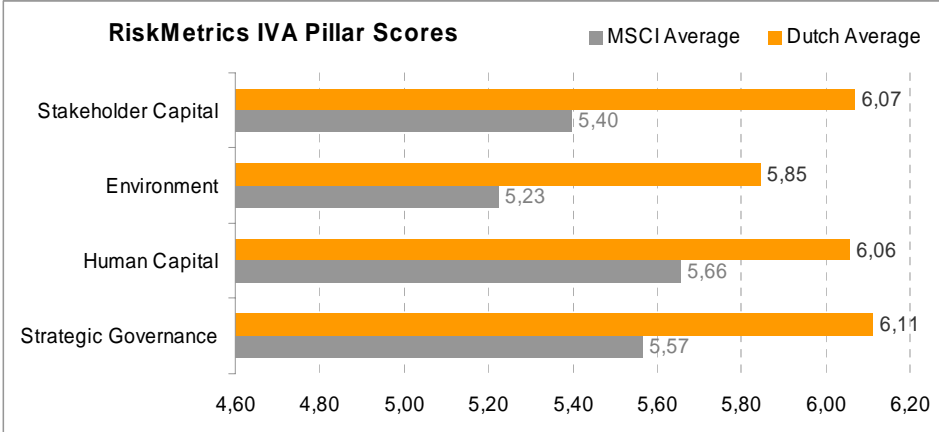
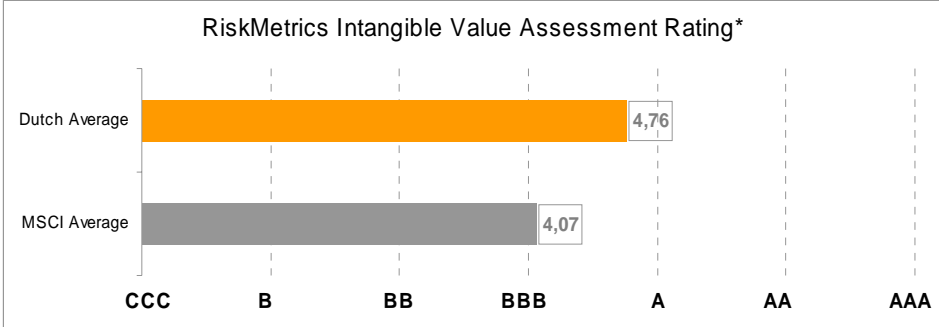
<sup>8</sup> Please also be referred to best practice provision II.1.2, under point d, where it is stated that the management board shall submit for approval to the supervisory board corporate social responsibility issues that are relevant to the enterprise.

In its explanation to the Code the Frijns commission refers to the Burgmans committee’s report on the relationship between corporate social responsibility and corporate governance and states that it considers the recommendations of the Burgmans committee to be a valuable addition to the Code and a logical elaboration of the Dutch corporate governance model.

In December 2008 the SER published a report on International Corporate Social Responsibility, in which it calls on companies to develop and disclose comprehensive international supply chain policies based on ILO, OECD and International Chamber of Commerce standards. The SER plans to monitor companies’ performance in this area on an annual basis. We can therefore see that the scrutiny of Dutch companies’ performance on ES issues is growing steadily. Furthermore, it is likely that expectations in the Netherlands relating to companies’ performance will become more demanding in the future.

*ES performance of Dutch companies*

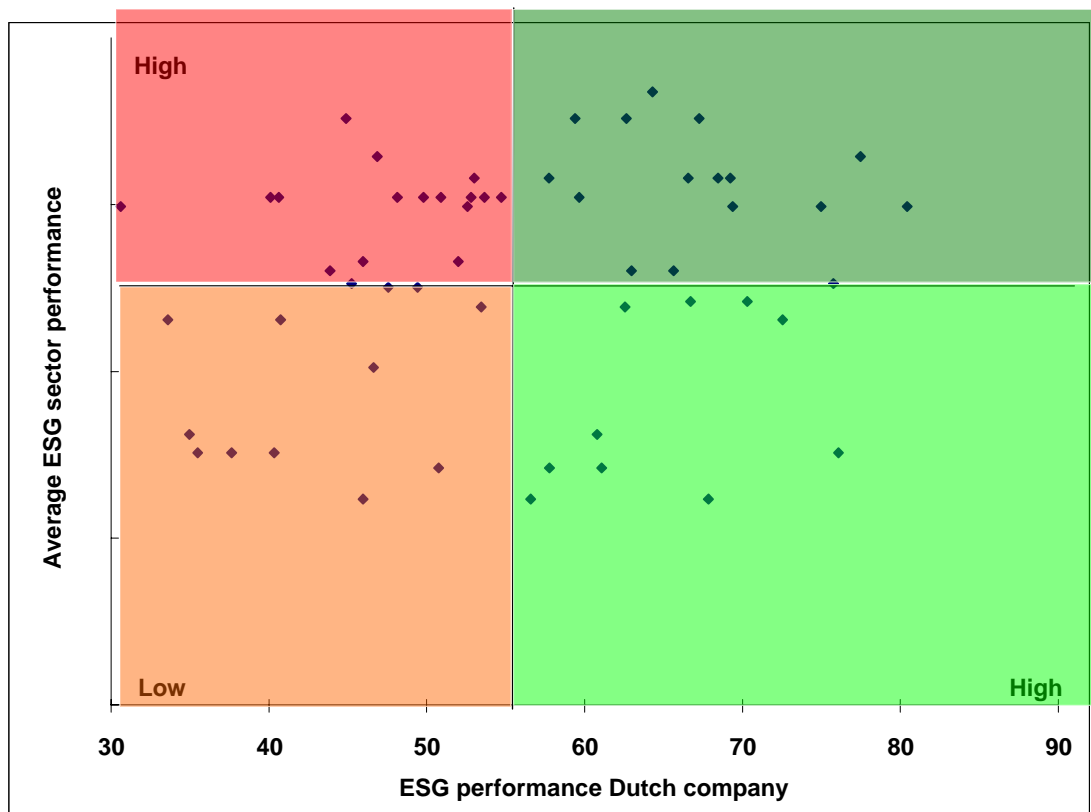
The ES performance of Dutch companies is in many cases superior to that of those in other countries. This is illustrated by the two charts below, comparing Dutch companies’ ratings in the Innovest sustainability rating system with those of companies in the MSCI World index. The first chart shows the companies’ overall ratings; the second shows ratings for individual dimensions of ES performance under the RiskMetrics system: stakeholder capital; environment; human capital and strategic governance.





Key:

- Stakeholder Capital – covers issues such as relations with communities and customers
- Environment – environmental policies, management and performance
- Human Capital – treatment of employees
- Strategic Governance – overall policy and strategic approach to ES issues.



RiskMetrics data only covers Dutch companies that are included in the MSCI World index. Research provider Sustainalytics (previously known as Dutch Sustainability Research-DSR) also covers smaller Dutch companies. Sustainalytics conducts extensive research and analysis on 2.000 companies worldwide and calculates scores for each of the themes Environment, Social, and Governance. The scores included in the chart above refer to the aggregated company sustainability score.

The chart above shows Sustainalytics' sustainability scores for all major Dutch listed companies in relation to the impact of sustainability on the sector they operate in. Companies plotted above the horizontal line have activities in sectors with a high sustainability impact. Companies positioned to the right of the vertical line have a higher than average company sustainability score. It is also noteworthy that a large number of smaller companies have a below average score and are located to the left of the vertical line. The chart clearly demonstrates a wide variance within Dutch companies with regard to their score on sustainability.

Finally, an assessment of ten of the largest Dutch companies by Goldman Sachs shows that, on the whole, Dutch companies perform relatively well, compared to their sector peers, on the management of their social risks, such as workplace safety and community investment. Dutch companies perform less well on the management of their environmental risks, with areas of particular weakness being use of energy and water, and greenhouse gas emissions.

## 2.2 Should investors in Dutch companies play a role in ES issues?

Investors have and should play a role with regard to ES issues, because first of all, it is in their own interest to ensure that all material risks are being managed properly and that opportunities are exploited. Increasingly studies and experience from academia and institutional investors demonstrate that ES issues could impact the value of investments, both positively and negatively. Neglecting to look at such factors could be seen as a failure to discharge formal obligations to beneficiaries or clients. Secondly, increasingly it is being expected by beneficiaries of pension funds or clients of asset managers to integrate ES issues in investment decisions and behaviour. This could involve clients' and beneficiaries' values as well as financial arguments. Thirdly, this is increasingly expected by other stakeholders such as NGOs and media. Neglecting to integrate ES issues could destroy an organizations' license to operate. In short, there could be legal, financial, and reputational reasons for investors to play a role in the field of ES issues.

The box below provides examples of investor initiatives on ES issues in a number of countries.

### *How are investors responding to ES? An international perspective*

A number of investors, in the Netherlands and internationally, have responded to the growing evidence that ES issues are relevant by developing their own capability to understand the issues and their implications for the companies they invest in. At the international level various initiatives have been taken.

In the **UK**, for example, the Association of British Insurers has been at the forefront of pressing companies to improve ES disclosure, while the government has published guidance for companies on how to incorporate these issues into annual reporting under the EU Accounts Modernisation Directive. The Directive requires companies to provide in their annual reports an "analysis of ESs aspects necessary for an understanding of the company's development, performance or position."

In **Germany**, DVFA – the Financial Analysts' and Asset Management Association – has published a set of environmental, social and governance key performance indicators that it believes all companies should use in order to enable investors to assess the financial relevance of companies' policies and performance on the issues.<sup>9</sup>

In **Norway**, a group of investors with a total of €326 billion in assets under management, supported by the government, has launched the Sustainable Value Creation project to encourage improved performance and

<sup>9</sup> [http://www.dvfa.de/files/die\\_dvfa/kommissionen/non\\_financials/application/pdf/KPIs\\_ESG\\_FINAL.pdf](http://www.dvfa.de/files/die_dvfa/kommissionen/non_financials/application/pdf/KPIs_ESG_FINAL.pdf)

disclosure by Norwegian-listed companies on issues including the environment, corruption, human rights and labour standards.<sup>10</sup>

The **CFA Institute** – the global professional body for chartered financial analysts – has recently published *Environmental, Social, and Governance Factors at Listed Companies: A Manual for Investors*, to enable investors to get to grips with ESG issues more easily.<sup>11</sup>

The **United Nations Principles for Responsible Investment** is a set of six principles<sup>12</sup> on the integration of ESG factors into investments that is now supported by 480 signatories with approximately 18 trillion USD AUM (as of April 2008). The principles are designed to provide practical guidelines for incorporating environmental, social and corporate governance issues into current investment practice and investment decision-making.

The **International Corporate Governance Network** has a committee on Non-Financial Business Reporting that has recommended a framework for company reporting on non-financial issues, including ES issues that are material to company financial performance and shareholders' interests.<sup>13</sup>

The above is relevant for any investment globally. So what is so specific about the Dutch market? There are at least two specific situations in which it is in investors' interest to engage with Dutch companies on ES issues.

Firstly, companies that currently underperform their peers in other countries would serve their investors' interests better if they improved their performance. This applies, for example, to the companies whose performance is shown in red in the Sustainalytics chart above.

Secondly, as we have seen above, many Dutch companies (particularly larger ones) are international leaders in corporate social responsibility and the integration of ES factors into these business practices. As we have also noted, outstanding management of ES risks and opportunities is in investors' interest. Investors can and should engage with these companies to ensure that they continue to lead the pack in international terms. Dutch companies could also set an example for other companies in investors' portfolios. This is especially true of those in emerging markets, though it is not confined to these companies.

#### *Existing Dutch ES engagement experience*

One Eumedion member met with the management board of one of the leading Dutch electronics companies to evaluate how environmental and social targets were incorporated into the company's long term strategy, risk management systems and remuneration policies. The company aims to increase revenue from "green products"

<sup>10</sup> [http://www.klp.no/web/klpno.nsf/pages/EnglishPressReleases.html?open&disp\\_key=44BD2329E1B1E7C0C12574A3002EDA](http://www.klp.no/web/klpno.nsf/pages/EnglishPressReleases.html?open&disp_key=44BD2329E1B1E7C0C12574A3002EDA)  
BA

<sup>11</sup> <http://www.cfapubs.org/toc/ccb/2008/2008/2?cookieSet=1>

<sup>12</sup> [www.unpri.org](http://www.unpri.org)

<sup>13</sup> [http://www.icgn.org/organisation/committees/committee\\_output.php?id=6](http://www.icgn.org/organisation/committees/committee_output.php?id=6)

to 30% of total revenue by 2012, and to improve the energy efficiency of its products by 10% with each new product release. At the same time, the company has outsourced much of its manufacturing operations to China, where environmental and labour standards tend to lag those of developed markets. Over the last several years, the Eumedion member, along with other stakeholders, encouraged the company to develop a supplier code of conduct that would commit the company to meeting certain minimum social, environmental and ethical standards throughout its supply chain. The Eumedion member questioned the company's commitment to these targets in light of the current economic downturn. It queried whether "green product" targets would be revised down given an overall slump in consumer spending. It also probed whether the company was seeing a deterioration in supplier performance against its standards given pressures to reduce costs, that could ultimately jeopardise its value chain. Lastly, the Eumedion member asked how remuneration targets were aligned with sustainability targets as well as overall financial targets. The company reported that its commitment to its sustainability targets remained unchanged. In fact, despite an overall fall in sales, revenue from "green products" increased from 20 to 25% of total revenues in 2008. Similarly, the company reported that it had sustained its commitment to managing environmental and labour standards risks in the supply chain and had reduced its timetable for resolving non-compliance issues by 60%, leaving it with a reliable and robust supplier base to sustain it through the downturn. Both targets are also reflected in remuneration targets linked to the annual bonus.

This experience shows that dialogue on environmental and social issues is often tied to a company's core business and can be a good indicator of overall corporate health and risk management. Engagement on ES issues over time can lead to significant improvements in corporate responsibility practice, and to the development of a corporate strategy that reflects broader macroeconomic pressures. In general, experience in the Netherlands shows that engagement can serve investors' interests, and promote wider corporate responsibility, in relation both to companies that are already well-advanced in their management of ES issues, and to those that are less highly advanced and may face financial risk and public scrutiny of their performance. Companies in the forefront should be stimulated to maintain their position whereas less advanced companies should be stimulated to improve their performance.

### **2.3 Should investors work together on ES issues?**

Given the relevance of ES issues to investors' interests that we have seen above, collaborative action by investors on these issues may be justified and beneficial in the same way as applies in the case of corporate governance issues.

Collaborative action is justified and indeed required in situations where a particular change in practice by an individual company or by the market as a whole is in the interest of all investors in that company or of investors as a whole, and where investors acting together are more likely to bring about that change than one investor acting alone, or individual investors acting in an uncoordinated way. It is self-evident that a group of investors acting together is able to bring greater influence to bear than a single investor acting alone. Collaboration widens and deepens the pool of skills available to achieve a given objective. This collaboration should take place internationally and nationally. In the Dutch context, collaboration would be a visible platform to demonstrate to Dutch stakeholders that Dutch investors take ES issues seriously not just internationally but also in their home market.

### *Investors' collaboration on company disclosure*

For investors to be able to integrate systematically sustainability factors into investment risk analysis there is a need for a high level of company disclosure on ES risks, and for quantification wherever possible. Investors need to have standardised data to evaluate and compare conduct of companies that could help identify investment risks. One standard that can be followed is the Global Reporting Initiative. Despite the fact that more and more Dutch companies use the Global Reporting Initiative Guidelines to report their ES performance, there are still no objective and standardised data available to truly compare conduct and quantify environmental, labour and human rights risks.

It would therefore be of benefit to investors as a whole if companies were to standardise their ES reporting. Standardisation would also be in companies' interest, since responding to inconsistent information requests from different investors is costly and inefficient. Collective action by investors in relation to ES disclosure would therefore lead to collective benefit to both investors and companies. This is the rationale underlying many of the existing collaborative investor initiatives on ES issues, including those in the UK, Germany and Norway referred to above.

There is therefore a case for collaborative action by investors in Dutch companies on ES issues of relevance to the market as a whole, and in specific cases on issues that are significant for individual companies.

## **2.4 What should investors expect of companies in the area of ES risk management?**

This paragraph deals with the rights and expectations investors have of company behaviour in the area of ES risk management. What investor should expect from companies logically raises the opposite question as well. What should companies expect from investors? Every right means a corresponding responsibility. The responsibilities investors should take into account will be addressed as part of the next section which deals with the possible role for Eumedion in such cooperation between investors, and the practical consequences thereof.

Primarily, investors seek evidence from all companies – in the Netherlands and elsewhere - that they are aware of the ES issues that can affect their operations, and that steps have been taken to address these. To this end, companies need to demonstrate their awareness of all key risks potentially affecting their operations, including the longer-term risks such as climate change, through a transparent risk assessment process. Following this, companies need to develop the following mechanisms to address issues considered to be of potential risk:

- On a group-wide level, companies need to recognise the significance of environmental and social risks threatening their operations, and develop clear **policies** addressing these. The policies should enable investors to understand clearly the company's stance on the issue, as well as the commitments the company undertakes with regard to addressing or mitigating the impacts of the issue.

- Any policies addressing ES risks need to be underpinned by transparent and comprehensive **management systems**, which enable investors to assess the steps the company plans to take to implement the policy. Where possible, the management systems should be based on international good practice standards, such as the ISO14001 standard for environmental management systems.

- Investors, but also other stakeholders, need to be able to assess the companies' **performance** in the management of key ES risks. To this end, companies need to develop measurable performance indicators, monitor their performance on an ongoing basis, and report on this information. The use of international reporting frameworks, such as the Global Reporting Initiative or the Carbon Disclosure Project, is helpful in facilitating cross-sector comparisons and alignment with international good practice.

- Needless to say, none of the elements of ES risk management described above can be assessed by investors and other stakeholders without high levels of **transparency**. Companies need to ensure that all elements of their risk management systems are publicly disclosed, and that progress in addressing them, as well as any ongoing risks and challenges, are disclosed periodically. The use of international reporting frameworks, such as the Global Reporting Initiative or the Carbon Disclosure Project, is helpful in facilitating cross-sector comparisons and alignment with international good practice.

## **2.5 Conclusion**

It is thus clear that a growing body of evidence suggests that ES issues are financially relevant to companies and therefore closely linked to investors' interests. There is increasing investor activity on these issues both within individual countries and through international networks. Collaborative investor initiatives have the potential to be an efficient way of pooling resources and maximising effectiveness in monitoring, analysing and influencing companies. As such there is a strong case for institutional investors in the Netherlands to collaborate on environmental and issues. Whether Eumedion could or should play a role here is the subject of the next Section.

### 3. Eumedion and ES

#### 3.1 What could be the possible role of Eumedion in ES cooperation?

The mission of Eumedion is related to corporate governance. According to Article 3 of the Constitution of Eumedion this mission is to maintain and further develop good corporate governance on the basis of the responsibility of institutional investors established in the Netherlands and to advance the acceptance of and compliance with generally accepted corporate governance standards by listed companies and institutional investors in the Netherlands and Europe in particular.

Eumedion endeavours to achieve this mission by (1) encouragement of joint consultations between institutional investors and with listed companies and their representative organizations (2) consultation with the Dutch government, institutions of the European Union, other relevant authorities and sectoral organizations (3) influencing legislation and regulations (4) providing services in the field of corporate governance to its participants and (5) other activities that advance the objectives of Eumedion.

Article 1, section 1, under point b, of the Constitution of Eumedion defines corporate governance as” *“the system of practices applied by a listed company in dealing with the stakeholders directly involved with the company and its business – in particular executive and supervisory directors and providers of capital –comprising a number of rules for good governance and supervision, and rules on the allocation of tasks, responsibilities and powers, leading to a balance of influence among those involved with the company and its business”*.

The text of Article 1, section 1, under point b, of the Constitution of Eumedion does not seem to hinder the broadening of the mission of Eumedion to ES issues, as a broad interpretation of the definition of corporate governance would also cover ES issues. However, in practice these issues are not covered by the current activities of Eumedion and this was also not intended when Eumedion was established. Therefore the current activities of Eumedion are limited to a more traditional interpretation of corporate governance.

Below the potential (dis)advantages of broadening the mission of Eumedion to ES issues will be described. Arguments in favour of broadening the mission of Eumedion are:

- (i) Corporate governance comprises the structures and systems for defining, managing and reporting on business risks, among other things. To be effective, corporate governance needs to consider all risks to the business across all parts of the business. By definition, management and reporting of ES risks therefore form elements of corporate governance. The level of priority and the form of the governance of ES issues need to reflect the relative significance of ES risks in the context of wider business risks. Many companies are increasingly recognising that ES issues, at a strategic level, are significant in terms of reputation, market opportunities, licence to operate and business efficiency. ES issues, in totality or as specific issues, are difficult to manage successfully in the long term if they are not

integrated into corporate values and governance. Increasingly companies understand the organisational significance of ES issues in a strategic and operational context. As a result, companies are starting to integrate ES issues into their values, operations and their corporate governance. This provides a strong framework within which managing ES issues can be prioritised, planned and conducted in the wider business context. It also enables ES issues to be better integrated into corporate behaviour to achieve sustained performance and results. Therefore the corporate governance framework is a potential framework to integrate ES risks and opportunities and there is an interest to cooperate within Eumedion.

- (ii) External expectations for ES management continue to evolve. This is evident through the activities of the Dutch government, the Burgmans committee, the Dutch Monitoring Commission on Corporate Governance, the Social Economic Council, who are all, in some form increasingly establishing expectations for demonstration of a response to ES issues. The Dutch government has demonstrated an ES agenda and has formulated the wish to promote ES. The government wants to inspire (awareness), innovate and integrate<sup>14</sup> on ES issues. Institutional investors can contribute to the development of the awareness of the importance of managing ES business risks. Opinions in society and on the capital market evolve so quickly that it is to be expected that current practices will not be deemed acceptable in the future. A broadly-based and coherent representation of interests can have added value in the field of ES issues. Eumedion can help or influence these expectations.
- (iii) The rise of ES issues on the governance agenda is best demonstrated through the publication of the revised Dutch corporate governance code, that stipulates that the role of the management board is to manage the company, which means, among other things, that it is responsible for achieving the company's aims, the strategy and associated risk profile, the development of results and corporate social responsibility issues that are relevant to the enterprise. "The management board is accountable for this to the supervisory board and to the general meeting of shareholders"<sup>15</sup>. It will therefore be more and more expected that shareholders and institutional investors in particular, will exercise their rights in order to make companies apply the new best practice provisions in the revised Dutch corporate governance code. This and the complex and integrated nature of ES issues require an adequate response by the participants of Eumedion. When there is reason to do so, institutional investors should pro-actively encourage the companies in which they invest to improve performance in these areas.
- (iv) The pressures on companies to manage ES issues and on investors to encourage the companies are also increasingly apparent through other stakeholder involvement. Institutional investors manage other people's money and therefore have a fiduciary duty with respect to their beneficiaries or investors. Several institutional investors experience pressure from those

---

<sup>14</sup> Please see letter of the state secretary of economic Affairs to the Dutch Lower House, dated 19 February 2009.

<sup>15</sup> Please be referred to best practice provision II.1.



beneficiaries and investors to critically monitor the management of ES issues by the companies in which their money has been invested. This is reflected by the fact that several participants of Eumedion have asked Eumedion to broaden its mission to ES issues, as they consider these issues to be significant factors in their investment policies where collaboration with other investors is desirable/necessary. Demonstrating an appropriate response to these demands is necessary to maintain a licence to operate from beneficiaries. Broadening the mission of Eumedion could contribute to more confidence by the beneficiaries and participants of Eumedion.

- (v) Managing ES issues is becoming increasingly important in companies' strategy and risk management. In 2009, risk management is again one of Eumedion's spearheads. It is expected that in 2009 there will be discussion on remuneration policies of financial institutions due to the financial crisis. Several companies are working on the integration of ES issues in the remuneration policy and are taking the ES aspects into account when formulating performance criteria. Risk management and remuneration are subjects that are an integral part of Eumedion's core mission. ES issues will become more integrated with corporate governance issues and Eumedion has to be prepared for that. Integration of ES issues within the Eumedion governance platform would then be a natural and logical step. If participants of Eumedion want to discuss these issues this can be done in a joint exercise with governance issues via the platform of Eumedion. One integrated platform reflects that ES factors could be considered as aspects of corporate governance and that it is best practice to integrate ES governance into the wider corporate governance structure and instruments.
- (vi) ES covers a wide range of topics which many times have an international dimension. Working together at a national level strengthens the role of investors in international platforms/networks. Taking ES issues seriously in the home market is an essential condition to be effective outside the home market. A coordinated response can be a more effective response.
- (vii) One integrated ESG platform of participants of Eumedion is the logical point of contact for the listed business community and other parties, such as media, the Monitoring Committee, political parties and social organizations that want to know the ideas of institutional investors. Eumedion has been accepted as the platform for institutional investors in the Netherlands for corporate governance and has also a growing international reputation. Eumedion has a good record, reputation and expertise. Engaging with companies would be easier if this would be done with other participants of Eumedion due to the good reputation of Eumedion. Coordination by and/or cooperation within Eumedion also avoids duplication of efforts of participants and could ensure full coordination and integration between governance and ES performance. In order to retain Eumedion's strengths, it would be advisable not to create another platform for institutional investors. Eumedion already has experience with the

coordination of general meetings as well as with lobbying the Dutch government and the European Union. Participants could benefit from this expertise, instead of creating extra costs and efforts in building up a new platform. Collaboration within Eumedion could therefore also lead to achievement of cost-efficiencies for institutional investors.

Arguments against the broadening of Eumedion's mission are:

- (i) Eumedion is currently strongly associated with the traditional interpretation of corporate governance and has a very good reputation. This reputation could be lost if ES issues were advocated by Eumedion. Different Eumedion participants will have different views about relevant ES issues and how to deal with these. Eumedion participants could face difficulties in formulating a shared view of what constitutes a risk and appropriate management of that risk because of the breadth and complexity of ES issues. This would mean dealing with subjectivities in risk assessment and the unpredictability and variability of ES risks and the lack of a widely accepted and concrete ES standard. This could undermine Eumedion's present good reputation.
- (ii) Broadening the mission of Eumedion would mean a much broader scope of issues to be dealt with by Eumedion, adding capacity and therefore additional costs (for example to hire new employee(s) with the necessary depth of experience in a very broad field). This entails the risk that some of Eumedion's participants may reconsider their membership of Eumedion.
- (iii) Companies with an international presence, conducting business in other countries and or with internationally outsourced activity have to manage and report ES issues in the context of their global operations. The real ES issues are therefore not necessarily related to Dutch companies or the Dutch domain itself, but have an international dimension. Broadening the activities of Eumedion to the management of ES issues by Dutch listed companies would not ensure a level playing field and some Eumedion members would therefore object. Some might argue that collaboration on such problem areas would be better organised at an international level, such as within the UNPRI, and not at a national level.

### **3.2 Conclusion**

After weighing the arguments in favour of and the arguments against extending the mission of Eumedion to ES issues, the working group concluded that it must acknowledge the great diversity/complexity of ES issues. In order to take into account the objections of participants that are critical about the broadening of the mission of Eumedion, it is important to recognise the differences in local cultures, legislation, priorities and needs when formulating the ES areas in which Eumedion should have a role. Therefore a realistic and pragmatic response appropriate for Dutch listed companies should be considered.

Eumedion is a corporate governance forum and ES issues are increasingly becoming a factor in risk management and business strategy, but also in the remuneration policy. ES risks can have a financial impact on a company and effective management of ES risks and opportunities can therefore improve financial results. From a corporate governance point of view, it is therefore important that companies manage these risks. Within the corporate governance framework board members and directors have a responsibility to address ES factors as their key board duty is the consideration of long term corporate risks. Their competencies and their ability to assess ES risks and strategy in this area is critical for effective governance and corporate performance. This is also demonstrated by the principles and best practice provisions on ES issues in the Dutch corporate governance code.

In this light, there is a case for cooperation within Eumedion on ES issues if these issues are relevant to long term value creation and can be raised at the general meeting of shareholders. The current Eumedion mission should be broadened to ES issues that fall within Eumedion's current corporate governance framework. For now, this means focusing on risk management, disclosure and remuneration policy related to ES issues that are relevant to shareholders. With the term "disclosure" the working group indicates its expectation for companies to be open on the ES issues that are relevant for shareholders.

The limitation to the corporate governance framework prevents Eumedion from losing itself in the broader ES domain which is very wide and complex. Specifically, this also means that ethical issues that are not related to risk management, disclosure and the remuneration policy currently fall outside the scope of the Eumedion activities.

Future development may lead to evolved or changed opinions of participants of Eumedion. In order to make sure that changes of opinion are taken into account, the activities and developments around the broadening of Eumedion's mission to ES issues should be evaluated at the end of 2010. When evaluating Eumedion's position, further developments or improvements could be considered.

### **3.3 Does ES fit into the daily business of Eumedion?**

It is important that the current strengths of Eumedion should be built on further. Cooperation on ES issues could be given form at collective level and at an individual level. At collective level participants of Eumedion could cooperate by involvement in policy making and policy engagement on ES issues and the formulating of the so-called Eumedion annual spearheads letter. At an individual level, cooperation could be given form by cooperation with regard to a particular company (general meeting of shareholders) as currently is being done with regard to the general meeting of shareholders on corporate governance issues. The key areas in integrating ES in the organisation of Eumedion would therefore be (1) policy making and policy engagement (2) cooperation on the coordination and preparation of general meetings of shareholders, and (3) building a knowledge centre on ES issues.

*Re (1) Policy making and policy engagement*

Currently, Eumedion responds adequately and quickly to new developments in the field of corporate governance and takes a stance where required. Eumedion advocates its vision on corporate governance, whether invited to or not, and influences legislators and regulators in the field of corporate governance. This also includes spreading the Eumedion vision to other relevant parties. Eumedion has a pro-active approach to policy making and policy engagement.

The working group agreed that Eumedion should also respond to policy making and policy engagement with regard to ES issues. However, this focus should be limited to the local Dutch context, Dutch ES legislation or regulation and, as for its current spearheads, to risk management and the remuneration policy. By limiting the policy making and policy engagement to the Dutch domain, duplications could be avoided with international platforms. In doing so, participants of Eumedion may get involved in debates on ES issues in The Netherlands on a timely basis. As corporate governance in the narrow sense is primarily regulated nationally, whereas ES issues are far more internationally oriented, Eumedion should not be pro-active in policy making and policy engagement on ES issues. The approach of Eumedion to ES policy making and engagement should for now therefore be reactive instead of pro-active. This will be evaluated at the end of 2010.

Furthermore, at collective level Eumedion participants annually formulate so-called spearheads for that season and the strategy to be pursued at the general meetings of shareholders in advance of the annual general meetings season. Eumedion sends this so-called spearheads letter to (approximately 75) Dutch listed companies. In this spearhead letter ES issues should be covered also when necessary and related to risk management, disclosure and the remuneration policy.

*Re (2) Cooperation on the coordination and preparation of AGM's*

The current services provided by Eumedion are focused on facilitating voting by participants at the general meetings of shareholders, in order to contribute to the role of institutional investors as shareholders. The activities of Eumedion in this context include monitoring corporate governance developments at listed companies, providing its participants with corporate governance information, and providing the individual participants the platform to discuss developments and issues with regard to a certain (general meeting of shareholders) company. In this context, the Eumedion participants that visit general meetings of shareholders take into account the Eumedion spearheads. These participants may also collaborate, meaning that they share information and views on the agenda items of a general meeting of shareholders (taking into account acting-in-concert limitations, etc) and give proxies to each other where desired. In 2009, Eumedion has also developed an alert service. In case of an important deviation by a listed company of Dutch corporate governance legislation, the revised Dutch corporate governance code, the Eumedion spearheads letter, or the Eumedion Corporate Governance Manual, members of the Eumedion Investment Committee first will discuss this deviation. After consultation with the involved company, Eumedion will send an alert to all its participants if it is not convinced by the company's explanation, asking for attention for this deviation.

These Eumedion activities with regard to a specific company or with regard to the agenda items of a general meeting of shareholders should where necessary and appropriate also be carried out with regard to ES issues.

### *Re (3) Knowledge centre*

Eumedion currently helps participants increase their knowledge and experience in the field of corporate governance as one of Eumedion's tasks is to increase the awareness of participants with less experience. Eumedion tries to raise the level of knowledge of participants by the following means:

- Research. Eumedion defines subjects for research in the field of corporate governance, reviews research and/or has research carried out that advances the quality of and compliance with good corporate governance. Such research could also be carried out in the field of ES issues, if there is a relation with risk management, disclosure or the remuneration policy.
- Monthly newsletter. Eumedion prepares a newsletter once a month, containing the latest developments in corporate governance in the Netherlands and in the European Union. The newsletter examines noteworthy issues at listed companies, Eumedion's stated positions, national and European legislative initiatives, and developments relating to the Tabaksblat Code. Eumedion will cover relevant ES issues in its monthly newsletter, if there is a relation with risk management, disclosure and remuneration policy related to ES issues that are relevant to shareholders.
- Participants currently are informed immediately of corporate governance developments in the Netherlands that are of major importance to institutional investors. Such developments may be related to events at individual listed companies (with the emphasis on the Dutch AEX and Midcap shares) or might refer to legislation and/or regulation. The alerts may lead to further action on the part of Eumedion, ranging from the facilitation of contact between institutional investors about the events in question, to the drafting of letters to policy-makers. Eumedion will take into account its new mission and will also send information regarding relevant ES issues or developments, if there is a relation with risk management, disclosure and remuneration policy.
- The Corporate Governance Manual was last amended in 2008 and will be revised when necessary. The Manual assists institutional investors amongst others in drawing up their own voting policies and in reporting on this. The Manual is forwarded to participants free of charge. Eumedion will take into account the new mission when it next revises its Manual.
- Symposia, seminars and workshops. Eumedion organises (at least) once a year a symposium on a corporate governance subject of contemporary interest. Eumedion could also do so in the field of ES issues, if there is a relation with risk management, disclosure and remuneration policy.

## **4. Practical consequences for the internal Eumedion procedures**

### **4.1 Eumedion committees and ES expertise**

The extension of the mission of Eumedion will have limited consequences for the internal Eumedion procedures. Eumedion currently has five committees, viz. the Legal Committee, the Audit Committee, the Research Committee, the PR Committee and the Investment Committee. The preparation of policies and the implementation thereof takes shape in these various Eumedion committees, the most important of which is the Legal Committee. The engagement, preparation and coordination of individual issues with companies or with regard to the general meeting of shareholders of companies take place within the Investment committee. Remuneration policy issues of a specific company are discussed in the Investment Committee where the policy issues on remuneration are discussed in the Ad hoc Committee Regarding Directors' Remuneration.

The current Eumedion internal organisation could stay unchanged. It is not necessary to create a new separate committee on ES issues as these issues will have a relation with the current corporate governance framework of Eumedion. The integration of the new broadened mission could then be covered by the current committees. It is important to mention that it will be the individual participant's responsibility to monitor whether their representatives on the committees sufficiently take into account ES issues. Furthermore, it is important that all current committees evaluate whether there is sufficient ES expertise within the specific committee. The ES working group agreed that it should meet after a period of one calendar year in order to evaluate the progress that is made on the integration of the new ES mission.

### **4.2 Eumedion Constitution and Charters of Eumedion Committees**

Due to the fact that the new mission will have a relation with the current corporate governance framework of Eumedion, it is not necessary to amend the text of the mission of Eumedion as expressed in Article 3 of the Constitution of Eumedion. However, the operational objectives of the different committees of Eumedion as expressed in the Charters of these committees should be amended.

## **5. Recommendations of the working group**

Having considered the aforementioned arguments, the working group advises the General Board of Eumedion to broaden the mission of Eumedion to include risk management, disclosure and remuneration policy related to ES issues that are relevant to shareholders by integrating it into the existing Eumedion committees and that the Charters of these committees be amended. The working group finally recommends employing one experienced staff member with specific ES expertise.

## **Annex: Members of the working group**

Else Bos (PGGM), Chair

Rients Abma (Eumedion)

Erik Breen (Robeco)

Kris Douma (Mn Services)

Marcel Jeucken (PGGM)

Anna Krutikov (F&C)

Rob Lake (APG Asset Management)

Henk Marius (Shell Pension Fund)

Bas Rüter (Triodos Fund Management)

Zöhre Tali (Eumedion)