Delivering sustainability and social impact through community engagement.

A people-centred approach to ESG

Roundtable, Paris 26-27th September 2023

Summary Report

Key findings

1. European legislation on social impact reporting and human rights due diligence is a ‘game-changer’. European policymakers and standard setters are creating a paradigm shift in terms of corporate accountability for environmental and social impacts. The scope and requirements of new legislation and the possibility of civil liability and redress mechanisms have implications for individual business leaders.
    i. Key industries in the European Commission’s spotlight to test the new legislation are extractives, the garment industry, tech companies and the financial sector.
    ii. Extended supply chains that include high risk areas are a particular concern for both regulators and companies.
    iii. More collaboration particularly between companies within sectors is required, to generate practice change; a partnership strategy from the European Commission would also encourage further systematic change.

2. There is a lack of quality local data to assess social impacts.
3. Community engagement is critical to managing both social risks and leveraging opportunities for positive impact but is under-emphasised by the legislation and current practice; dialogue with affected groups from unions to communities is needed to overcome pockets of resistance to new practices around climate transition.
4. Confidence and trust-building is a key, but missing, component in both environmental and social action by business.

5. Many companies are focusing on risk management in addressing social issues, particularly in FCS. Fewer are focused on the potential for positive transformation. Risk management and positive action should not be seen as binary, rather a continuum within corporate strategies.
6. There are positive examples and experiences of mainstreaming social action and innovation and engagement with communities, that need to be better known to encourage other companies.
7. There are lessons from environmental reporting and the Paris climate goals that can be used to strengthen social impact accounting and strategies and to bring about the Just Transition.
8. The lack of a social impact metric hinders the development of S in ESG compared to environmental impact management.

Aims

The roundtable brought together companies, investors, policymakers, and standard-setting bodies to identify best practices and policies for achieving positive social impacts and sustainability goals through investments and operations across the supply and value chain and particularly at local level in fragile and volatile environments.

New European legislation on sustainability reporting, mandatory human rights due diligence, and increased attention by financial markets and rating agencies on the social impacts of business have increased pressure on companies to provide information about their social footprint, including in locations where they may have little direct representation.

The Just Transition agenda includes a social dimension to action on net zero and climate change agendas. The roundtable sought to discuss how engagement with communities and local stakeholders could be made more effective and useful for companies and investors; how accurate and authentic information could be integrated into reporting, and address risk and opportunity locally, and the kind of support companies and investors need to adapt to new regulatory and public demands on social impact.

The in-person roundtable was held over two days for invited participants with an online link for companies who were only able to join virtually. The roundtable comprised [x] participants overall. It was held under Chatham House rules to facilitate free discussion.

The context for change in social impact and community engagement practices by the private sector

European legislation was described frequently by participants as a 'game changer' in influencing corporate behaviour and an increased focus on environmental and social issues. Lucrezia Busa, Adviser to the EU Commissioner for Justice and Consumer Protection ·said legislation on human rights and the Corporate Sustainability Reporting directive (CSRD) marked a clear shift from voluntary to mandatory measures, and the new legislative initiatives – which are being matched by national legislation in member states such as France and Germany – were part of a rolling programme lasting until 2028, to strengthen European level competence. The programme will involve monitoring companies' entire value chain in order to identify risks and provide remedy to protect both people and the environment. The Commission's aim is to create a level playing field in Europe, provide legal certainty and to be consistent with European values, using the Commission's economic powers to align with its political objectives. The legislation aims to target the riskiest situations which occur beyond Tier 1 suppliers, and monitoring and enforcement will focus initially on sectors such as mining/extractives and the footwear and garment industries, with the financial sector also emphasized as a key lever to achieve protection and responsible business conduct. The Commission is considering enforcement and redress/remediation mechanisms, alongside incentivising company directors to implement new reporting and accountability measures and will issue guidance and implementation measures to help companies comply.

UN Global Compact underlined the need to shift from voluntary to mandatory changes in business conduct. UNGC is stepping up its guidance and implementation initiatives, although warned that companies are overwhelmed by new reporting requirements, and this risks under-action rather than real change.

A representative of [Morningstar Sustainalytics](), a leading global ratings agency, underlined their use of a double materiality approach, looking at social impact as well as financial metrics. Nordic companies have particularly embraced this approach. The agency is planning an impact weighting rating for companies based on social and environmental factors. Analysis adopts a value chain approach covering Tier 1 and 2 suppliers and looks at both positive and negative impacts. The biggest constraint on their impact analysis is the lack of on-the-ground data about social incidents and impacts, particularly in areas where there is limited civic space or historical data. There is a need for investors to be proactive rather than reactive and to engage at community level rather than only use delisting as a means of regulating corporate behaviour; the slow speed of data gathering, and a lack of human-centred analysis limits the quality of assessments.

Key challenges for business

Companies raised the following issues guiding social impact practice:

Supply chains are critical to making people's lives better or worse, but these chains are often complex for example in the automotive industry, so companies struggle to trace their impacts.

Individual responsibility is an increasingly important theme and collaborative action is also needed, but companies operate within their own silos and don't talk to each other and there is a lack of systematic thinking and practice across companies in relation to sustainability and social impact. There are more efforts to strengthen collaboration between companies and suppliers. There are examples (chemical industry and ENEL – Italian energy company) where supplier engagement programmes have created dialogue, support and training. However, there is still an important gap in terms of the focus on local communities – they are not seen as a key stakeholder to talk to or for bringing a unique perspective and route to meaningful engagement.

In high-risk areas and sectors simple compliance is no longer enough to achieve positive impacts.

There is a distinction between managing local risks in the supply chain – which most companies see as necessary – and aiming to create positive social impact as part of a wider responsibility and sustainability strategy. The two perspectives are usually seen as binary rather than part of a continuum of outcomes.

Stronger sectoral initiatives are needed –examples in palm oil and jewellery- are useful. The European Commission needs to focus on partnership to help the shift in behaviour.

LSE IDEAS study for KPSRL identifies that most companies don't measure positive social impacts; legislation and practice are predominantly shaped by human rights norms so no guidance on capturing positive impacts, or operationalizing stakeholder engagement particularly in difficult settings where there is no RoL.

The study examined the value of local engagement, the kinds of indicators of successful engagement and how this might fit with existing standards, noting that it is difficult to transfer the different frameworks and standards into measurement practices consistent with strong local engagement.

Trust and credibility are key concerns, with business and CEO's not trusted relative to government or to people placing trust in themselves, to respond to climate change, according to the Edelman Trust Barometer. Incidents of disputed advertising campaigns illustrate that companies can no longer make 'lazy green claims', and that greenwashing is an important issue. In the absence of any regulatory authority the Science Based Target Initiative (SBTi) attempts to help companies report emissions data for environmental reporting. Problems with the initiative include inability to check the accuracy of reported data or third-party verification.

Ways forward

The human security approach proposes four kinds of value creation:

1. Learning – a way to know and understand the local context
2. Relational – generating better interactions with communities
3. Instrumental – generating better processes including impact measurement
4. Financial – leading to better returns and profitability.

Considering whether social innovation can be a realistic goal, it was suggested that more incentives – fiscal, educational and training – are needed, as well as data comparisons, to encourage positive action. Actors such as ESG rating agencies are significant in driving business behaviour change, but do not offer a ***theory of change***. Practices such as exclusionary screening by investors and ratings bodies and the lack of connection between the principles behind normative standards and actual outcomes, do not focus on positive transformations. There is a risk that there are too many global standards and legislative initiatives.

Two presentations focused on how to operationalize social innovation and connect top-down initiatives on environment and social impact with the grass roots conditions at community level. French consultancy KSAPA identified key problems as

- internal resistance from traditional profit centres inside businesses who see no incentive in accelerating climate transitions;
- resistance from trade unions who see the shift as creating complexity and new processes;
- a gap in communication with vulnerable workers who need to have global goals such as Net Zero translated into realities such as livelihoods and resilience.

Overcoming resistance will require better planning by companies and policymakers and more training and education. Incentive structures also need to consider the role and responsibilities of business in social transformation; the role of governments is being blurred by the new legislation.

Suez Group set out their social business approach – a bottom-up strategy based on the ideas of a circular economy and social innovation. The principles behind the approach are:

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  - Business solves problems and can have a disproportionate impact compared to NGOs
  - No green transition is possible without reducing social inequalities
  - The green transition requires multi-stakeholder partnerships and coalitions at ground level
  - Tech innovation is not enough. Social innovation is quicker to achieve and can be found in new business models, contract management and social areas.
  - employees are powerful change agents and can foster positive impact.
- The Suez strategy works through tailoring commercial products based on new solutions and partnerships with 'complementary actors' such as social entrepreneurs to help them scale projects; an inclusive approach to recruitment, purchasing and HR planning and a 'beyond business' philanthropy initiative to encourage employee volunteering and strengthen Suez's contribution beyond its business

Presenting 'Resources for managing local impacts. A human security approach' Mary Martin, LSE IDEAS, highlighted the gap between expectations on business and tools available to them to manage and report on social impacts at local level.

Research conducted by the UN Business and Human Security Initiative found that social impact management is a fragmented field, with each company adopting its own processes and trying to find individual solutions.

There is a *conceptual* challenge around the meaning of S in ESG? What does good practice look like?

There is a *practical* challenge related to data – what data to use and how to understand it

Local social impacts are particularly problematic to assess and manage:

- Companies rarely know all the parts in their global value chain, issues can result in significant, and potentially criminal harms
- There is a need to put people back into the equation, integrating the human element, beyond just aggregated numbers
- This requires:
    - Granular, up to date information
    - Robust and meaningful local engagement
    - Working with diverse stakeholders
    - Sustained and structured dialogues
    - Adaptable strategies

- Based on insights from the Human Security Business Partnership Framework, the ***Human Impact Pathway*** would propose steps to enable companies to
  - Gather and use local information.
  - Manage risks and Identify opportunities.
  - Report and measure impacts in specific contexts
  - Through close, sustained and structured engagement with local stakeholders

Rabobank highlighted a major credit lender's experience with environmental accounting and reporting highlights the following issues:

- The need for a process of continuous learning in which norm-setters, including ESG ratings agencies and lenders work with corporates
- The need for a scientifically based measurement to drive target setting linked to both short and medium-term actions
- The value of leveraging the advocacy role of banks and other lenders to drive change in behaviour
- positive encouragement is more productive and realistic than negative actions such as delisting or exclusions
- Incentives can be based on pricing discounts (better loan rates for example)
- The value of 'sustainability dialogues' and relationships between corporates, credit analysts and lenders