Chapter Zero
The Directors' Climate Forum

CASE STUDY

Climate leadership in the boardroom

Introduction

Boards of directors are under increasing pressure to understand and respond to the risks and opportunities of climate change. This is driven in part, by the factors that influence business behaviour on any issue, the expectations of stakeholders and the policy and regulatory landscape. In addition, the personal implications individuals on the board may face if they don't steward the company through the challenges caused by climate change also plays a part. An increase in litigation against directors, shareholder activism, public scrutiny and the toughening of some governance codes has led to a greater sense of individual accountability for climate risks in the boardroom. This is a complex and fast-moving challenge for boards to contend with. We've witnessed a marked shift in how they have been and are engaging with climate change as a result.

Leadership is a key driving force behind the development of corporate climate plans and the lack of board prioritisation is one of the significant barriers to progress identified by respondents. From the responses, over half cited executive motivation an important driver for change but the role of the board was less evident. Given the strategic role the board plays in enabling businesses to develop and implement effective climate transition plans, the value of its leadership should not be underestimated.

Board leadership is critical to driving business transition in four areas: strategy, governance, ambition and incentivisation.

Key messages

The changing external landscape and responsibilities of board members mean their engagement and leadership are critical in shaping how climate change is integrated into business strategy.

The scale of transformation needed means climate change must be embedded in all parts of governance, with the whole board taking responsibility for the strategy, with aspects of it supported by individuals and committees.

Climate change doesn't necessitate that the board has topic experts in its membership, but it does need to have enough competence to oversee the creation and delivery of an ambitious and robust climate plan.

Incentives linked to the climate plan connects the prosperity of the company with the risks posed by not acting on climate change and ensures there is a clear structure for accountability.

01 Board accountability for climate change and strategy

The board and its members are responsible for ensuring 'the company's prosperity by collectively directing the company's affairs, while meeting the appropriate interests of its shareholders and relevant stakeholders'.[1] This means setting the vision and values of the company, defining the strategy, overseeing its management and how it is implementing plans, and monitoring ongoing success.

Climate change impacts businesses in a number of ways and therefore influences these responsibilities. In the longer-term, the board may decide to engage in significant transformation. But there are also immediate physical and transitional risks. Notably, as the links between climate change and financial risk have become more apparent, the expectation that businesses disclose the risks they are exposed to has ramped up. The adoption of the Taskforce on Climate-related Financial Disclosure (TCFD) principles by governments and financial regulators has been one of the key forces driving greater board engagement with the issue.

Considering these responsibilities and external influences, the board's engagement has become critical in shaping how climate change is integrated into the business strategy, how that is implemented and reported on, and in setting out an ambitious vision for the future.

Our climate programme is fully aligned to and influences the overall organisational purpose and strategy. Initiatives are integrated within wider business activities and the operating model. The Board has increased oversight not just from a compliance perspective, but also on how performance is measured and improved. The Senior Vice President of Sustainability sits in the global executive and is involved across board matters.

RB (Consumer Goods)

02 Embedding climate into governance structures and committee functions

The scale of transformation needed within business to reduce emissions to the levels required means climate must be embedded in all parts of governance. While integrating climate change into the strategy should be a whole board responsibility, individuals and committees will be responsible for aspects of it. Likewise, aspects of the strategy need to be vertically assigned to the appropriate internal teams, as well as horizontally supported through cross-functional working.

The emerging role of the Chief Sustainability Officer (CSO) reflects a move away from climate and sustainability being an add-on activity, towards being something that is central to decision-making and governance.

From respondents, it is clear that the support of executive functions like the CEO or CFO is fundamental for driving climate action. However, the non-executive directors (NEDs) are an equally important group. They fill most board seats, and their independent nature means they can radically influence the nature of a board discussion, particularly if more than one NED is driving the climate agenda.

With the emergence of the CSO, there has also been a movement to establish Sustainability Committees or equivalents, which are often responsible for the detailed background thinking needed to inform the board's decision-making.[2]

We have a governance and compensation committee at the Board level involved in our sustainability charter. From the Sustainability Office, Group Executive Council, Business Leadership, Facilities Management Group, Infrastructure Creation Group, HR, Finance, Corporate Affairs, Marketing and Risk Office, each has a set of sustainability responsibilities against which they are measured.

Wipro Limited (General Services)

1 Standards for the Board, IoD
2 Chapter Zero, August 2021, What we've learned from Sustainability Committee Chairs

Initiatives in our change programme are driven by committees that both set targets and execute against them. Our Board of Directors provide the strategic guidance on sustainability, our Group Executives are accountable for our sustainability programmes and they appoint: our Compliance Committee; Sustainability Committee; and, QHSE (Quality, health, safety, and environment) Committee. The Sustainability Committee set our targets, review our strategies and manage performance. Environmental Policy Committee execute programmes, whilst assessing their viability.

Ørsted (Energy, Resources & Utilities)

03 Overseeing ambitious targets and robust plans

The board is accountable for making sure that the ambition the company has to reduce emissions, is based on where its impacts are created (including all scopes) and where it needs to adapt or increase resilience, with targets supported by a robust plan and short-term milestones.

This plan must include the steps necessary to ensure the organisation has a culture to support its transition, that teams are empowered to act, that capital is allocated in the right areas and that opportunities for innovation or growth are maximised.

For board members, setting the right metrics to understand what is happening across the business is key to an effective oversight role. Using these as the basis for reporting, including acknowledging where gaps remain or where challenges exist is now expected from business and goes beyond merely a compliance exercise.

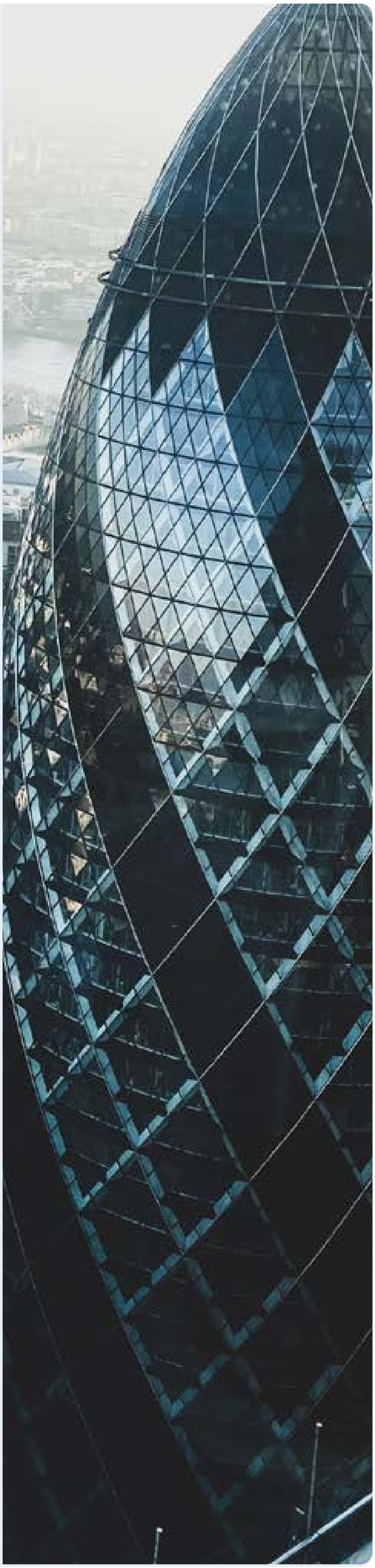
The board should recognise that transparency about progress is important in the success of the climate plan as this helps engender confidence among stakeholders. Likewise, communication both internally and externally is increasingly important if a company is to get the buy-in needed.

While board composition is an important part of effective climate governance, few boards have sustainability or climate experts within their membership[3]. They should instead be focused on building broad competence of the subject, drawing on the expertise of employees and external advisors as plans develop. This will support successful implementation as the plan is founded on a realistic understanding of what is possible for the business.

Our overarching climate strategy at the CEO level, is core to the Purpose of our organisation, which in turn underpins our strategy and the decisions we make on the future direction of the business. This ensures that targets and activities are ambitious enough to meet strategic objectives, which is further supported by our governance measures, which are tied to climate performance.

NatWest Group (Financial Services)

3 The Sustainability Board Report 2020, The Sustainability Board Report



04 Incentivising leadership to deliver

Aligning climate targets with executive compensation and remuneration is becoming increasingly common. The board should ensure that 'executive incentives are aligned to promote the long-term prosperity of the company including climate related targets'.[4] This directly links the prosperity of the company with the risks posed by not acting on climate change, and ensures there is a clear structure for accountability.

While performance-based incentives are one approach, another complementary one is to drive the internal change by recognising team or departmental progress. Linked directly to the integration of a climate strategy vertically within the business, finding ways to incentivise and reward progress internally (while avoiding the creation of unhealthy competition) can accelerate bottom-up progress.

We have introduced an internal carbon fee mechanism of $15 per metric ton on all carbon emissions, which was doubled in 2019. This internal "tax" was established in 2012 to hold our business divisions financially responsible for reducing their carbon emissions. The carbon fee is set each year based on the estimated cost of internal efficiency, renewable energy, carbon offset, e-waste recycling, and other innovative research projects to be carbon neutral.

Microsoft Norge (Telecommunications, Media & Technology)

The increased drive towards transparency and the scrutiny companies find themselves under means that the board is incentivised to deliver. If directors are ultimately responsible for climate change action, they are also responsible if the company fails to deliver.

Accountability for our senior leadership is through our long-term incentive plan. Our CEO led the launch of the targets and has taken ownership for the topic. Ultimately the Board level CSR committee, Executive leadership team and board of directors are accountable. We have introduced a carbon reduction metric into our long-term management incentive plan alongside EPS and ROIC – a move that was driven by CCEP's board-level remuneration committee.

Coca-Cola European Partners (Consumer goods)

Chapter Zero
The Directors' Climate Forum

Chapter Zero, the Directors' Climate Forum, is building a community of non-executive directors and equipping them to lead crucial UK boardroom discussions on the impacts of climate change. Its 1,700+ members are helping ensure their companies are fit for the future and that global net zero ambitions are transformed into robust plans and measurable action.

Established by a group of non-executives in 2019, Chapter Zero offers its members tailored events, toolkits, relevant information and a peer network to draw on for experience, inspiration and ideas. Visit **www.chapterzero.org.uk** for more information.

4 How to Set Up Effective Climate Governance on Corporate Boards: Guiding principles and questions, World Economic Forum.