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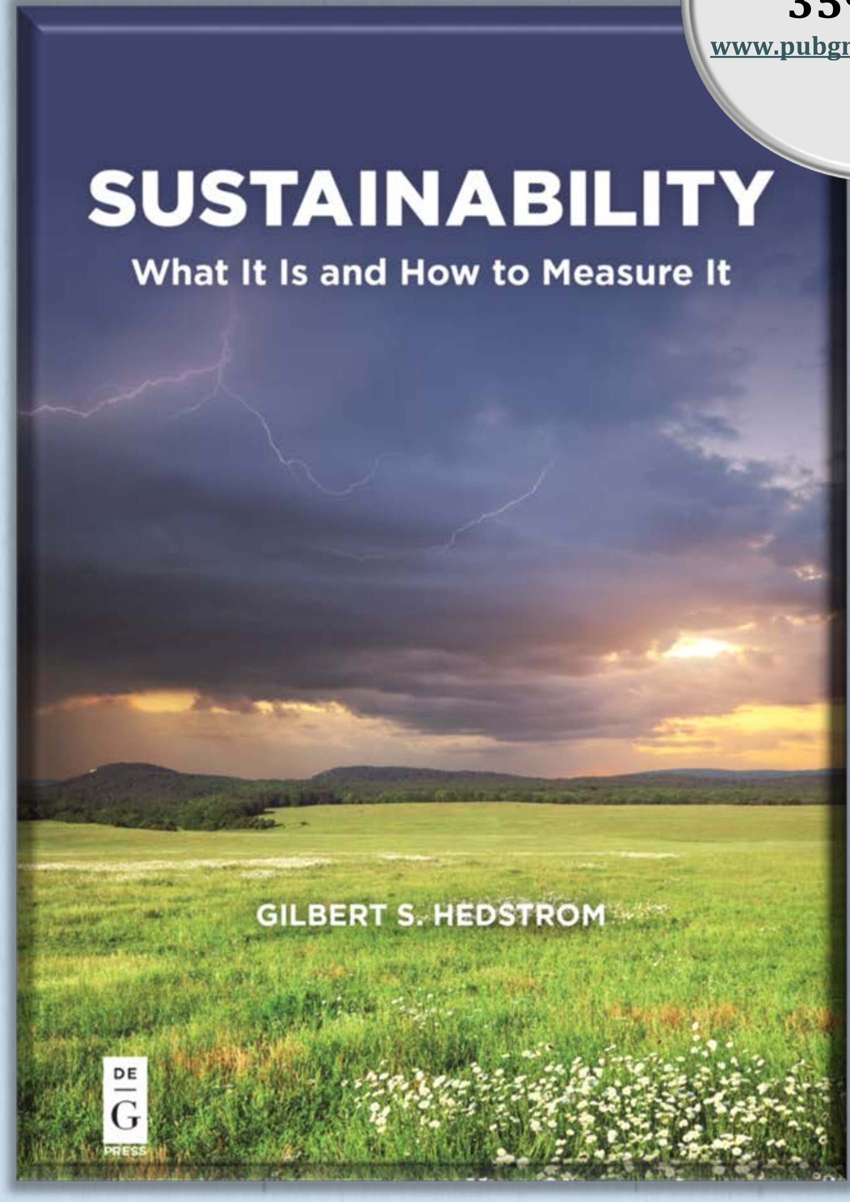

SAMPLE CHAPTER

Introduction to the Corporate Sustainability Scorecard—C-Suite Rating System

Advance Praise

The authoritative book on the most vitally important issue of our day.

— Ken Tierney, Group Vice President, Sustainability
Sims Metal Management

A must read for every business leader who wants an organized, comprehensive summary of sustainability—packed with industry best practices.

— Dave Stangis, Chief Sustainability Officer
Campbell Soup Company

I highly recommend this book to senior leaders who want to understand quickly why sustainability matters to your business and how to measure it. The book also provides a great overview of the current trends around sustainability strategy and governance.

— Karen E. Koster, Executive Vice President
Hexion, Inc.

Building a sustainable enterprise can be a complicated journey, but one made much clearer by Hedstrom's concise primer and valuable roadmap. The book draws on rich examples across industries, and will help boards and executives move faster toward managing risks and harnessing the opportunities of sustainability.

— Jason Jay, Senior Lecturer and Director
MIT Sloan Sustainability Initiative

The challenges facing society and the environment today are unprecedented. Businesses embracing sustainable development will gain competitive advantage and better manage risk. The book provides a balanced, insightful, unbiased review of sustainability—and the Scorecard is a terrific tool to help business leaders gauge how they stack up today.

— Lori Michelin, President and CEO
World Environment Center

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About the Author

Gilbert (Gib) Hedstrom has over thirty years of experience advising CEOs and board members about how to handle difficult environmental and business challenges. After twenty years at consulting firm Arthur D. Little, where he was vice president and managing director, Gib launched Hedstrom Associates in 2004. Gib provides consulting services to companies about issues that lie at the intersection of corporate governance, strategy, and sustainability.

Gib has reported to full boards of directors or board committees (with oversight of corporate responsibility issues) of major global corporations on over sixty occasions. In his role as independent sustainability advisor, he counsels directors concerning the risks and opportunities, and shares examples of "best practices" globally. He often meets with outside directors in "executive session" (without members of management present).

His clients have included Accenture, AES, Air Products, Alcoa, Ashland, Autodesk, Bayer, Baxter, Boeing, BP, Calvert, Coca-Cola, Conoco, Cytec, Dell, Ford, HP, Honeywell, Kodak, Monsanto, Novartis, Novo Nordisk, Pemex, Raytheon, Sask Power, Shell, United Technologies, USG, and United States Steel, among many others.

For The Conference Board, Gib serves as program director of *Sustainability Council I: Strategy and Implementation, Sustainability Council II: Innovation and Growth,* and the *Chief Environment, Health, and Safety Officers' Council*. These councils provide the opportunity to interact with executives of about 100 leading companies—and to keep his finger on the pulse of current developments.

Gib has authored several books and written dozens of articles related to the environment, governance, strategy, and sustainability. Frequently, he is called upon to speak on business risks and opportunities created by environmental and social trends.

Gib has dual master's degrees from the University of Michigan (MBA Corporate Strategy; MS Natural Resource Management) and a BA (Economics and Geology) from Hamilton College. He welcomes further discussion about governance, strategy, and sustainability issues, and can be reached at gib@hedstromassociates.com.

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Contents

Chapter 10
Introduction to the Corporate Sustainability Scorecard—C-Suite Rating System

This chapter serves as an introduction to the Corporate Sustainability Scorecard. We encourage readers to also visit the website (www.thesustainabilityscorecard.com) to visualize the on-line tool.[1]

However, all of the detailed elements of the on-line rating tool (the back-end) are described in detail in the following chapters. In other words, as of the time of writing, Part 2 of this book (the following seventeen chapters) actually includes *more* detail than is in the back-end of the website.

This chapter outlines:
- What is the Corporate Sustainability Scorecard?
- Why this Scorecard?
- Who is the Scorecard intended for?
- How is the Scorecard structured?
- How do companies progress through the four stages?
- How should the Scorecard be used?
- Will the Scorecard change over time?
- How is Part 2 of this book organized?

What Is the Corporate Sustainability Scorecard?

The Corporate Sustainability Scorecard™ is a rating system developed by industry, for industry—to facilitate discussions in boardrooms and executive offices. The Scorecard is an on-line rating tool available to registered users. Visit: www.thesustainabilityscorecard.com for more information.

The Scorecard is designed to help companies answer the same question many CEOs and board members have asked the author: "How do we stack up today vis-à-vis sustainability as compared with competitors, best practices, and where leading companies are heading?" The Scorecard also helps executives map out where they want their companies to be tomorrow—given the competitive landscape, each company's ambitions, and the speed needed to win in the marketplace.

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1 The website has a "front end" that is visible to all and a "back-end" that is visible only to registered users of the Scorecard. Unless you are a registered user, you will not see the back-end at this time.

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An example of a summary scorecard for a typical company is depicted in Figure 10.1.

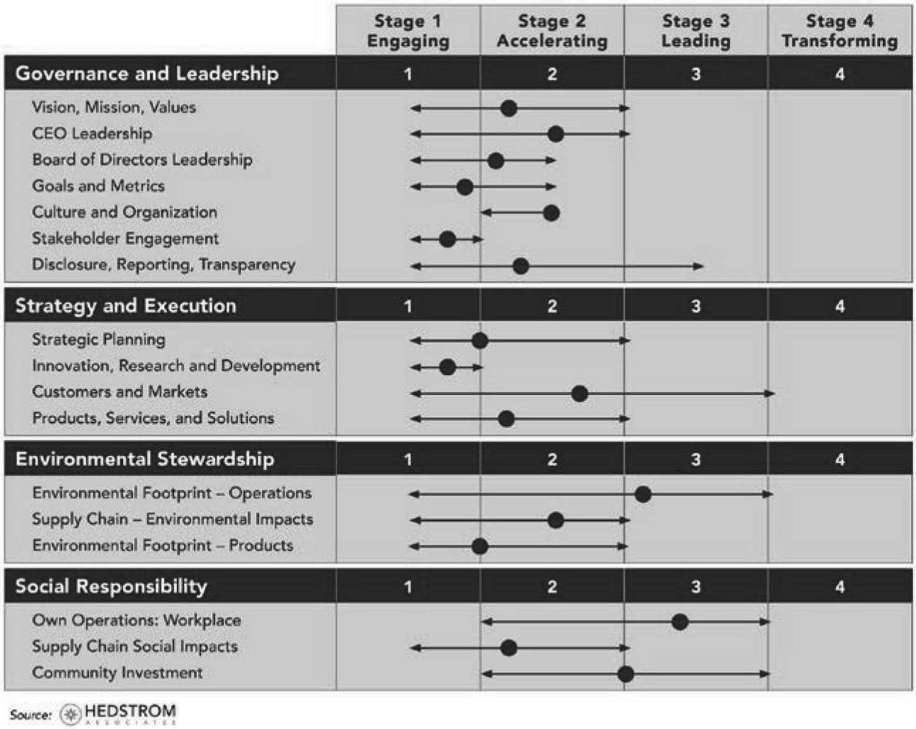

Figure 10.1: Example Corporate Sustainability Scorecard

Why this Scorecard?

There is no shortage of scorecards out there that companies are barraged by. Walmart has its scorecard. Dow Jones Sustainability Index and the various other corporate sustainability rating organizations each have some kind of template or methodology or scorecard to rate companies.

In stark contrast to the over 100 sustainability rating schemes in existence today, this Scorecard is focused on the aspects of running a business that matter most to boards of directors and C-suite executives. And, you rate your own company.

So why this one? Four reasons:

- *By Industry; for Industry.* The Scorecard has been used with the following companies in recent years: 3M, Air Products, Akzo Nobel, Anheuser-Busch, Ashland, Campbell Soup, Coca-Cola, Cytec, Deere, Dell, DuPont, Ford, Honeywell, HP, International Paper, Johnson & Johnson, Novartis, Novelis, Novo Nordisk, Pemex, Raytheon, SC Johnson, Shell, Sims Metal Management, UPS, USG, and Xerox. (Note: In some cases, the Scorecard was used as part of a Hedstrom Associates client assignment for the company; in other cases, the company used the Scorecard on its own.)
- *Full of Best-Practice Company Examples*. Several hundred examples are provided of companies that are considered to be in Stage 3 or Stage 4 for a particular attribute.
- *It Speaks the Language of the CEO and Board.* The seventeen individual elements that comprise the Corporate Sustainability Scorecard are purely business-focused. Each element (e.g., Culture and Organization; Strategic Planning; Innovation, Research and Development, etc.) is a major corporate function or activity on which CEOs and Boards of Directors spend considerable time.
- *Proven*. The Scorecard has been around for twenty years. In addition to the twenty-five to thirty companies that were involved with the Scorecard prior to 2016, an additional sixty major global companies all completed a company self-assessment in early 2018. These sixty companies found the Scorecard to be easy to use and applicable. They also provide some improvement suggestions that have been adopted in the on-line tool and are reflected in this book.

Who Is the Scorecard Intended for?

The Corporate Sustainability Scorecard™ C-suite rating system is designed for use by corporations—especially large corporations.

Though the Scorecard can be used by various individuals and groups within a company, the tool is designed primarily for use by (and discussions with) the executive team. Typically, use of the Scorecard is led by the officer who oversees internal sustainability efforts and reports to the CEO and Board of Directors (or Board Committee) about sustainability posture, programs, performance, and plans. The Scorecard places the entire sustainability conversation in a simple board-friendly context.

Corporate executives use the Scorecard to map their company's current position on a one-to-four maturity scale so that they can know with confidence:

- Where their company stacks up vis-à-vis sustainability (in other words, where they are on the maturity path)
- How their company compares with competitors and peers
- What "best practice" (defined as a Stage 3 or Stage 4 practice) looks like today

How Is the Scorecard Structured?

The Scorecard's summary table (depicted in Figure 10.1) is supported by a robust methodology. It is organized into:

- ***Four Parts.*** The four main sections of the Sustainability Scorecard include: *Governance and Leadership*, *Strategy and Execution*, *Environmental Stewardship*, and *Social Responsibility*.
- ***Seventeen Elements***. Within the four parts described above, seventeen topics (elements) comprise the overall Corporate Sustainability Scorecard.
- ***~150 KSIs.*** For each of the seventeen elements of the Scorecard, executives rate the company on eight to twelve "sub-elements" "KSIs." (Note: The current version of the Scorecard has 147 KSIs. The precise number may vary slightly over time based on feedback from registered users of the Scorecard.)
- ***~600 Descriptors.*** In each of the following 17 chapters, small tables define the four stages of performance for each KSI.

The Four-Stage Transformation Model

Engaging, Accelerating, Leading, and Transforming

The Scorecard rating scale is deliberately tough. This is not your traditional rating scale where Stage 4 is the top quartile of companies today. The bell curve on this Scorecard is skewed left, reflecting the fact that the vast majority of companies today are early in their sustainability transformation (see Figure 10.1).

As depicted in Figure 1.3, the vast majority of companies today are in Stage 1 and Stage 2. The fundamental premise behind this Scorecard is that sustainability is about transformation; that is, virtually every old-school company must transform itself to survive and thrive.

A brief synopsis of the characteristics of the four stages of transformation follows.

Stage 1: "Engaging"—*Stage 1 companies engage with sustainability issues in a variety of ways, although they do not change their company or their businesses fundamentally.* These companies undertake important efforts to reduce impacts and drive environment, health, and safety (EHS) and social responsibility excellence. Sustainability efforts are often driven by the chief EHS officer in collaboration with the officer leading philanthropy and corporate citizenship initiatives. Environmental stewardship and social responsibility are considered the "right thing to do." Environmental management is largely about risk management. Social responsibility is about worker safety and health, diversity, community responsibility, and philanthropy.

Stage 1 companies are committed to compliance—not just with laws, regulations, and internal company standards, but also increasingly with industry codes of practice and de facto requirements, including the **Global Reporting Initiative (GRI)** sustainability reporting guidelines and other nongovernmental organization (NGO) expectations. Stage 1 companies implement strong programs to reduce energy use, greenhouse gas (GHG) emissions, and waste in their own operations. They also respond to environmental and social pressures throughout their supply chain.

Stage 1 companies tend to interact primarily with their industry peers; and they typically support positions endorsed by their major industry associations. These companies may partner with external stakeholders on selected initiatives. Many, but not all, Stage 1 companies publish external EHS and/or sustainability reports (or the equivalent on their websites).

In summary, Stage 1 companies do many good things. However, when viewed in hindsight from those who are leaders, Stage 1 companies essentially "dabble in sustainability," while they continue to make the same products they traditionally produced. For example, many chemical companies continue to churn out the same chemicals while cutting energy use; consumer products companies keep selling the same products while "tweaking around the edges"—cutting a little water use or packaging content; oil companies continue to produce oil while driving operational efficiencies.

Stage 2: "Accelerating"—As a key characteristic of Stage 2 companies, *the CEO explicitly recognizes the potential significance of sustainability—and launches a few key initiatives to position the company as a leader on a business-critical aspect of sustainability*. In some cases, the CEO sees sustainability issues not only as a source of risk, but also as a source of potential opportunity.

What separates Stage 2 companies from their Stage 1 counterparts? Notably, the CEO of a Stage 2 company personally stakes out a position that addresses a "material" environmental or social issue faced by the company and its industry. A **material** issue (Appendix A: Definitions) is much more than an important issue. Many Stage 1 and Stage 2 companies publish a "materiality assessment" that may identify twenty to forty or more important issues. Yet, in virtually every case, a company has only a small handful of truly material ESG issues. (See Chapter 8: Environmental Stewardship for a further discussion of materiality.)

In some cases, Stage 2 companies set forth CEO-driven and bold sustainability positioning and goals. Many companies (e.g., Alcoa, AT&T, Campbell Soup, FedEx, Ingersoll Rand, and J&J, among others) have done this with their GHG reduction goals. The CEO and other senior executives may weave sustainability into public statements and speeches. In other situations, the company achieves a breakthrough position on a key issue facing its industry. For example, many Stage 2 companies took a lead role in addressing key industry challenges such as electronic waste. As Stage 2 companies advance, they build a culture that values sustainability-related innovation. For example, they may focus on stakeholder partnerships on a major social or ecosystem issue.

Stage 2 companies have well-defined environmental and social management systems, though those processes tend to be "*bolted onto*" (rather than "*woven into*") core business processes and business decisions. These companies have not changed their business models fundamentally.

Those in the manufacturing or process industries still largely operate in the traditional, linear, "take-make-waste" model, as contrasted with the new circular economy model. Those in the lighter footprint and service sectors remain focused on traditional customers, rather than also focusing on emerging middle class customers (at the bottom of the economic pyramid).

Stage 3: "Leading"—*Stage 3 companies begin to transform their business portfolios to leverage sustainability opportunities*. Moving beyond the few key CEO-driven sustainability initiatives of Stage 2 companies, the Stage 3 companies embody economist Joseph Schumpeter's concept of "creative destruction." They make strategic choices to divest "old economy" businesses and to invest in cleaner, greener, and more society-friendly enterprises.

Stage 3 companies take a longer-term view. They see the clean technology sector growing at double-digit rates—including products and processes that improve environmental performance in the construction, transport, energy, water, and waste industries. These companies want to be part of the "clean technology" revolution. They see massive growth opportunities in stabilizing atmospheric carbon concentrations, providing access to fresh water, and investing in smart cities. For example, more than any other major oil company globally, the French oil company, Total, sees electricity as a hedge against oil's eventual decline. Total is building a new business (akin to Ford's sustainable mobility business) around green energy, including batteries, solar, and other renewables.

Companies moving significantly into Stage 3 consider sustainability key to their organizations' long-term viability and value-creation. For example, NextEra Energy has made such a choice with its investments in renewable energy. Sustainability represents one or more platforms for top-line growth. Siemens sees the transition to a low-carbon economy as the biggest industrial challenge of this century. The company's *Environmental Portfolio* grew to almost half (46 percent) of the company's annual revenue in 2016. Stage 3 companies have a clear, focused strategy that places global environmental and social drivers at the core. They anticipate customer needs and future differentiators, as Toyota did with the Prius many years ago. A Stage 3 company is viewed internally and externally as open, transparent, innovative, and critically aware of risks and opportunities (e.g., SC Johnson and Nike have been systematically removing toxic materials from their products).

In making the decision to implement such significant changes, CEOs of Stage 3 companies begin the hard work of *weaving material ESG issues into the fabric of every critical business process, key business decision, and investment*. The key here is *material* as opposed to *important* ESG issues. For example, it is not likely material for a bank to reduce its water consumption, while it is material to change its investment criteria or lending policy to better reflect the ESG risks of its customers. This turns out to be a massive effort, as anyone close to the transformation of Novelis or Unilever can attest.

Stage 4: "Transforming"—*Stage 4 companies are evolving rapidly as models of twenty-first century corporations*. Those in the manufacturing or process industries (historically reliant on physical resources) live in the circular economy. For a pharmaceutical company, the issue is less about the circular economy and more about how many lives are improved as a result of access to medicines.

Sustainability is incorporated fully into the Stage 4 company's vision, mission, culture, business model, and goals. Each of these companies has a clearly defined roadmap for sustainable growth and profitability, which explicitly reflects the firm's responsibility to future generations. This commitment extends far beyond the CEO. In Stage 4 companies, *sustainability is integrated fully within all aspects of the business* as they move toward 100 percent renewable energy, closed-loop manufacturing, shifting from product to service to solution, and enhancing employee and community health.

The focus of these companies remains steadfast on long-term profitability and growth, while also helping to solving the world's toughest problems. Tesla CEO Elon Musk embodies many of these attributes, though not without some controversy. He points to Tesla's huge "gigafactory" in Nevada as a model for one way to *transition the entire world to sustainable energy*. At the same time, Musk may not have sufficiently addressed the disposal of lithium batteries and he also is criticized for focusing on space exploitation while there are giant problems on our planet crying for attention.

Though *no major company today is solidly in Stage 4*, a growing number of companies have some Stage 4 attributes. They fall into two groups: young, innovative, sharing-economy companies, such as, Google, and Tesla; and old-line companies, such as BASF, Philips, Siemens, Unilever, and Waste Management.

How Should the Scorecard Be Used?

As you consider where your company (as well as your competitors and customers) sits across the four-stage model, keep these points in mind:

- *There is no inherently right or wrong place to be on this continuum*. The Corporate Sustainability Scorecard focuses on progressing through various stages. "Right" or "wrong" depends on timing. Certainly, examples exist of Stage 3 and Stage 4 companies that have faltered, and of Stage 1 and Stage 2 companies that have looked wise in hindsight.
- *Don't be surprised if your company is largely in Stage 1*. The majority of companies find that many attributes of their company are in Stage 1 today—or were until fairly recently. Even if your company is predominantly in Stage 2 or above, the

chances are that you have many internal activities and core business processes that remain in Stage 1.
- *Moving at the right speed at the right time is essential.* Companies move at different speeds. DuPont began early and moved systematically from Stage 1 to Stage 3. *GE* decided in 2005 that it was "behind the game" and needed to leapfrog beyond competitors and peers as it moved very quickly from Stage 1 to Stage 3.
- *A key point to keep in mind.* While it is convenient to express a company as being "in Stage 1" or "a Stage 2 company," in reality, most companies exhibit a range of attributes that fall across several stages of maturity on this scorecard.

The Scorecard is designed not only as a tool, but also as a collaborative learning process. Companies have successfully used it in facilitated meetings of the C-suite, board, or a senior cross-functional team. Having identified very clearly how their company "stacks up" today, C-suite executives use the Scorecard to engage in a typically deep and profound discussion of how they want to position the company for future growth—leveraging the mega-trends impacting society.

Individuals can gain access to the online rating tool by visiting www.thesustainabilityscorecard.com and reviewing the various "Join" options. Individuals who meet the join criteria become a "registered user" and receive a username and password, providing access to the "back end" of the website with the full rating system.

Will the Scorecard Change over Time?

A final point: While the Hedstrom Associates team does not expect the fundamental structure of the Scorecard to change, we do anticipate that over time the individual KSIs—and the descriptors of those KSIs for Stages 1–4—will evolve. Moreover, we expect the hundreds of best practice company examples to change on a continuing basis. Users are encouraged to submit their own suggestions of a Stage 3 or Stage 4 practice (of their own company or of a company they admire). The Hedstrom Associates team will continue to update the downloadable scorecard templates periodically and provide those to registered users on www.thesustainabilityscorecard.com.

Organization of Part 2

The seventeen chapters that follow present the seventeen elements of the Scorecard. These chapters follow a similar structure:
- A definition of what is meant by the Scorecard element, the key question it aims to address, and an example of a company best practice
- A brief overview of how the individual key sustainability indicators (KSIs) are grouped under several headings

– Descriptions of the eight to twelve KSIs—including a small table defining the KSI and including brief descriptors of Stage 1 through Stage 4
– Bulleted lists of "best practice company examples" (which we define as being in Stage 3 or beyond) for each KSI
– Final thoughts on what the data shows from the initial group of companies completing the Scorecard

NOTE: The KSI numbering is off by ten, meaning that the next chapter is Chapter 11, dealing with the first element of the Scorecard. Thus, the KSIs in Chapter 11 and in each subsequent chapter are off by ten.

SUSTAINABILITY

Sustainability: What It Is and How to Measure It serves two distinct purposes that make this book most important for any business leader. First, it describes, in an unbiased manner, what sustainability is all about – explaining exactly how to think about the risks – and perhaps more importantly, the opportunities – associated with business sustainability. Second, it presents a complete system that enables you to measure precisely how your business stacks up against industry leaders.

The author includes in great detail his proprietary framework, The Corporate Sustainability Scorecard™ C-suite rating system, which has been developed over 20 years and used by more than 70 Fortune 500 companies. This invaluable tool is meant for internal use at your organization to evaluate its practices in governance, strategy, environmental stewardship, and social responsibility.

Gilbert S. (Gib) Hedstrom illustrates the use of the Scorecard with hundreds of best practice examples. He discusses the sustainability transformation that is sweeping across the business landscape today, framed in the language of the board and C-suite, but easily accessible to anyone with an interest in this most timely subject.

This important contribution to the sustainability debate is undoubtedly the most detailed examination of the metrics currently available to evaluate a company's management of environmental, social, and governance issues. Those interested in sustainability and business can learn from innovators around the world who are profiting from helping to solve the many problems that society faces today.

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