

## **Ethical Corporation Article**

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Rapid growth in superannuation (pension funds) in Australia has brought with it a new core driver of corporate social responsibility – the pension fund industry itself. In Australia employer contributions to employee superannuation funds have been compulsory since 1990. According to Macquarie Bank, Australia now has a superannuation pool of \$1.2 trillion, which makes it the country with the second largest pool of investible funds in the world, following Japan. And it's still growing.

This is good news for advocates of CSR. Increasingly, the organisations that manage these funds are beginning to take social and environmental considerations into account when assessing companies they choose to invest in. With a pool of \$1.2 trillion, it is clear that pension fund managers and trustees have the potential to become major influencers of corporate behaviour. They have the means to provide the next pressure point on business to drive increased standards of social and environmental responsibility. They can do so because they are by nature risk averse, and CSR strategies when successful mitigate new forms of social and environmental risk well before they appear in corporate profit and loss statements.

The government has also recognised the role that pension funds can play. The report of a Parliamentary Joint Committee inquiry into corporate responsibility that took place last year strongly encouraged superannuation trustees to consider companies' environmental and social responsibility because "it is in fact bound up in long-term financial success that a superannuation trustee would be closer to breaching the sole purpose test by ignoring corporate responsibility."

Fund managers should expect more questions from pension fund trustees about the social and environmental risks managed by the companies in which they invest. Some companies will wait for these questions from fund managers. Other companies already considered leaders in CSR can exert influence by supporting trustees in their quest to better understand their biggest CSR risks and challenges.

Disclosure of company's non-financial risks has been a key issue for the Australian Securities Exchange Corporate Governance Council, which has been accepting submissions from stakeholders in its review of its 2003 Principles of Good Corporate Governance. Amongst proposed changes is that Principle 7 should be revised to include additional reporting requirements in relation to environmental, social and governance risks, not just financial risks.

With the results due out any day now it will be interesting to see what comes from this. But one thing has already become apparent from the review submissions: the emerging disconnect between the investment community and listed companies on the disclosure of environmental, social and governance risks. Submissions from listed companies tended to favour an approach which would not effect major changes to the ASX's CGC's Principles. This was in contrast to the position espoused by many investors.

The Australian Council of Superannuation Investors, representing 38 industry superannuation funds, said "In order for investors to mitigate risks, proper disclosure of a company's environmental, social and governance risks is a vital first step." While the Investment and Financial Services Association said that "Investors now seem more convinced than ever before that how a company goes about identifying, assessing and managing environmental and social issues is central to good corporate governance".

So where will things go from here? Members of the pension fund community in Australia are increasingly making the "materiality linkage" between financial value and CSR issues. They are demanding greater levels of disclosure by companies and this information is being incorporated into their financial assessment of companies. Bob Welsh, CEO of VicSuper, speaking at a recent ACCSR event, suggested that pension funds and other institutional investors, step up to the plate on sustainability by establishing and publishing an engagement policy for investments in companies covering ESG issues, encouraging

companies to unlock the financial performance opportunities by adopting sustainable business strategies. And then, engage with companies.

Backed up by international innovative initiatives such as the United Nations Principles for Responsible Investment, the Enhanced Analytics Initiative and the Investor Group on Climate Change, it is clear that investors in Australia are taking on a more engaged, more activist role in building a broader range of ESG issues into their risk management and lending profiles. They are doing this, not because it may be the "right" thing to do, but because it builds long-term shareholder value. This is effectively changing the Australian landscape on CSR.

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