Timely Corporate Governance Actions for Addressing Climate Change

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This Special Issue on Climate Concern and Corporate Governance is indeed very timely and important. It acknowledges that climate change poses many complicated global-scale problems to ecosystems, economies, markets and businesses. Climate induced rising temperatures, and consequent melting ice, extreme weather events, rising sea levels and biodiversity loss will disrupt businesses and livelihoods. In the words of the editors, 'Climate change impairs social and economic inequities, heightening the need for *quick action*' [emphasis added].

I want to address what does 'quick action' mean in this context, and what sort of corporate governance could enable it. Earth's climate has been on a dangerous trajectory for the past century and was first brought to global attention at the 1972 United Nations Conference on the Human Environment in Stockholm. As early as 1990, the Intergovernmental Panel on Climate Change (IPCC), in its First Assessment Report, highlighted the dire global consequences of climate change. IPCC has issued five additional assessment reports to date, each report has confirmed the dire and growing deterioration in the Earth's climate. These have been confirmed by additional scientific reports by the National Academy of Sciences of many nations.

There is scientific consensus that climate change is caused by excessive carbon in the Earth's atmosphere which traps heat and causes global warming. Warming the Earth melts polar ice and permafrost, leading to the release of additional carbon, sea level rise and biodiversity loss. Historically, for the past several thousand years before the discovery of fossil fuels, the amount of carbon in the Earth's

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atmosphere was stable between 190 parts per million (ppm) to 270 ppm. Carbon dioxide concentration in Earth's atmosphere, by 1959, had grown to 316 ppm. By 2022, carbon concentrations had risen to 418.5 ppm, and in 2023 as high as 423 ppm have been recorded in places.

As Figure 1 shows, we are still going in the wrong direction with regard to carbon in Earth's atmosphere. So *quick action* now means 'acting immediately and accomplishing transition to zero carbon within the next decade'. Climate harm is already happening as evidenced by more frequent extreme heat events, increasing floods and wildfires and rising global temperatures. The Catastrophic impact of climate change may still be avertable by reducing carbon emissions starting now. Corporations as the main engines of our global economy are at the heart of controlling carbon and decarbonizing our economy.

Corporate actions are urgently needed to control many aspects of global carbon emissions. A key source of atmospheric carbon is fossil fuels. The global economy is still over 80% dependent on fossil fuels which are produced and used by corporations of many types to produce goods and services. Corporations prospect for fossil resources, extract them, refine them, create byproducts, sell them, use them, recycle them, and in the process, they release giga tons of carbon into the atmosphere. At every stage of the carbon cycle, corporations can directly influence carbon leaks and emissions. Corporations can stop climate change. They can

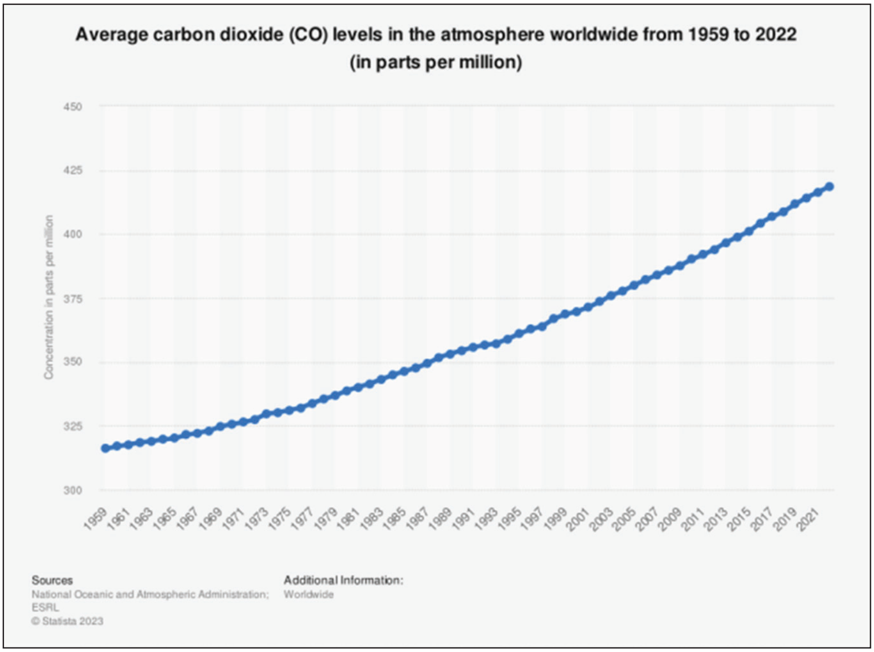

Figure 1. Carbon Levels in the Atmosphere.

transition from fossil fuels to renewable fuels, using proven technologies and financing arrangements.

Fossil fuel companies are planning on transitioning to renewables and blue hydrogen and reducing carbon emissions, but their visions for transition are over multiple decades. For example, Aramco, the world's largest carbon company, in its 2022 Annual Sustainability Report expressed its 'ambition to reduce our emissions by 52 MMt Co_2e and lower our upstream carbon intensity by 15% by 2035'. At this rate, the company will take half a century or more to reach zero carbon. This is action in the right direction, but this is not what I would consider 'quick action'. Other oil majors made ambitious promises for carbon reduction before COVID-19. However, they are walking back on those promises. In February 2023, BP scaled back an earlier goal of lowering its emissions by 35% by 2030 to a new goal now of cutting back carbon by 20% to 30%. ExxonMobil withdrew funding for a project to use algae to create low-carbon fuel. Also, Shell retracted an increase in its investments in renewable energy in 2023. Overall, the fossil fuel industry is slowing down its commitment to carbon reduction—this is not quick action (Noor, 2023).

In addition to reducing carbon emissions, corporate actions are also needed to create climate-resilient communities that can adapt to climate patterns that are already in play. Extreme weather events are causing damage at large scale and impacting many sectors of the economy. Climate is now responsible for 5 million excess deaths worldwide each year (Zhao et al., 2021). The insurance industry is paying out increasingly large damages each year for casualty and property insurance losses. In the State of Florida, nine insurance companies have stopped underwriting insurance because of past losses. In coastal areas, insurance prices are rising to unaffordable levels making communities less resilient (Cremades et al., 2017).

Good corporate governance is central to making corporations act on climate change. As hierarchically structured entities, the vision and ability to act are fundamentally determined by corporate governance arrangements. Despite our best intentions to reverse climate changes, most corporate governance initiatives have made only minor incremental voluntary changes. This has resulted in too little governance to control carbon emissions and a lack of accountability for climate change by companies. Incremental changes in governance are not likely to work in a timely manner to avert climate catastrophe, because they are simply too small. Voluntary operational changes are not likely to be successful since they try to preserve core business processes that need to be transformed. Corporate transformation to mitigate and adapt to climate change will require serious governance changes.

Let me propose a few bold actions that can improve corporate governance and address climate issues 'quickly'. We need meaningful governance with measurable results. Companies can move towards such responsive governance by using B Corp Form, Environment, Social and Governance (ESG) Investing, and adopting Sustainability Standards.

B Corp Form

The trade-off in balancing profit with ethical purpose at the governance level is addressed by the B Corp or benefits corporation movement. It was initiated by the non-profit organization B Lab founded in 2006. It seeks to transform the global economy to 'benefit all people, communities and the planet' by reorienting the very purpose of businesses towards sustainability. B Lab assesses and certifies companies that agree to follow guidelines for managing in ethically, socially and ecologically responsible ways. Companies gain B Corp status based on how they score out of 200 points on a variety of governance metrics, treatment of workers and customers and community and environmental programs. Companies must legally embed the B Corp commitment into their mission statement or get re-incorporated as a B Corp (a legal structure that formally embeds societal obligations into the company's goals). Globally, there are about 6,500 certified B Corp, including Ben & Jerry's Ice Cream owned by Unilever, Nespresso owned by Nestle, subsidiaries of French food group Danone, outerwear brand Patagonia, and Natura, the Brazilian cosmetics and fragrance maker that owns The Body Shop and Aesop.

Despite the popularity and growth of B Corps, they have not yet become mainstream. The current norm remains equity ownership defining governance priorities. In most companies, governance practices privilege investor priorities of maximizing profitability, paying out dividends and boosting stock value. Governance could be made more genuinely more multiparty by having employees, communities, climate science, consumers and other stakeholders be equity holders. This would result in balanced multiparty governance regimes to emerge, more capable of handling climate challenges in a balanced way, than one-sided (pro-investor) governance structures prevailing today. Employee Stock Ownership plans have been adopted by many companies to reward, motivate and empower employees. They could serve as a model for bringing in other stakeholders into ownership and governance arrangements.

ESG Investing

In the past decade, ESG Investing has become popular among investors and investment management companies, as a way to address climate change and sustainability concerns. Investors are seeking opportunities to invest in sustainable and ecologically responsible companies. Investment companies are assessing and factoring ESG risks into investment decisions to do more 'sustainable investing'. BlackRock Investments, the world's largest investing company pioneered the practice of ESG investing by incorporating financially material ESG data into firmwide processes, with the goal of enhancing risk-adjusted returns of clients' portfolios. They apply this universally in all portfolios, 'regardless of whether a fund or strategy has a sustainable or ESG-specific objective' (BlackRock, 2023).

Corporations have responded to demands for ESG improvements by reducing their environmental impacts, boosting corporate social responsibility initiatives and improving governance mechanisms. Most large corporations issue annual sustainability reports and use sustainability branding in their PR and communications outreach to customers and investors. Companies have adopted differing and non-uniform formats in reporting climate and sustainability data. So, it is hard to interpret and compare across companies. In general, corporate sustainability reports show year-by-year improvements in most sustainability parameters, such as carbon emissions, recycling efforts, safety and community engagement. Yet, at the global level, carbon in the Earth's atmosphere has continued to rise each year, as Figure 1 shows. So, there are concerns of greenwashing on the part of corporations.

Sustainability Standards

Corporate governance practices need to be fair and equitable across companies, industries and countries. For this, we need standards for climate and sustainability-related strategic and operating parameters and their reporting. The Global Reporting Initiative, founded in 1997, has evolved to provide uniform reporting guidelines. The ISO 14000 standard provides standards on some environmental and sustainability parameters. The newly created Sustainability Accounting Standards Board recently released its S1 and S2 standards in July 2023. They provide a common language, framework and variables for sustainability reporting by international corporations.

Sustainability governance practices are also advancing with a series of EU legislations over the past decade. The thrust of these legislations is on long-term transparency measures and on providing shareholders and stakeholders with timely information. This Shareholder Rights Directive was adopted in 2017. The Corporate Sustainability Reporting Directive revises corporate obligations and creates new ones on company disclosure and corporate governance. The November 2022 Directive on corporate boards' gender balance harmonizes and improves Member State practices regarding gender representation on company boards. Forthcoming (by 2026) is the directive on corporate sustainability due diligence mandates corporate sustainability due diligence duty to address negative human rights and environmental impacts by integrating due diligence into corporate policies and measures, directors' duties and remuneration (Huttunen, 2023).

To achieve meaningful governance over climate actions with measurable results, companies need to combine these above tools and other emerging ones. There are hard trade-offs that will need to be made. However, there are also strong synergies that could be beneficial for the long-term flourishing of companies. I hope articles in this Special Issue will provide guidance to make corporate governance truly effective.

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