

## Further proof that engagement works: the results of the second biodiversity benchmark

### Introduction

Investor engagement is increasingly recognised as an effective way of bringing about systematic improvement in companies' management of social, ethical and environmental issues. Insight has found that benchmarking is one of the most effective analytical and engagement tools. Here, we discuss our recent benchmark of 36 UK-headquartered companies in the extractive and utility sectors. (Prior to this we carried out two other benchmarks: one focusing on companies' management of supply chain labour standards and the other assessing UK house-builders' performance on sustainability).

### How does benchmarking work?

We start by establishing an analytical framework that articulates best practice on a given issue, covering companies' governance, strategy, policy management and reporting, as well as the use of specific tools, technologies and processes relevant to the issue at hand. This provides an objective and consistent basis on which to analyse and compare selected companies' performance. It also facilitates dialogue with management by identifying each company's particular strengths and weaknesses. Repeating benchmarks regularly enables us to track each company's progress over time.

### Biodiversity benchmarking: establishing the framework

Biodiversity-related<sup>1</sup> issues are increasingly relevant to the extractives and utility sectors. Natural resources are becoming more and more scarce, pressure to develop new resources to meet growing demand is mounting

and public concern about the loss of biodiversity is escalating. As a result, unless companies can demonstrate that they manage biodiversity issues effectively, they may face difficulties in the medium- to long-term in accessing resources in new areas and suffer competitive disadvantage relative to others with better practice. In the short term, their revenues may also be affected if they incur liabilities or their operating costs increase. They may also suffer reputational damage.

To assess the extent to which companies in which Insight invests were exposed to these risks, and how effectively the companies are in managing them, Insight launched its 'Biodiversity and Extractives' programme in March 2003. We started with a preliminary survey of a range of oil and gas, mining and minerals and utility companies to determine whether they had policies on 'sensitive sites' – sites with particularly high levels of biodiversity or at high risk of being lost or damaged.

We then hosted a seminar for these companies, representatives from government and biodiversity experts, to discuss the principles and standards according to which extractive and utilities companies should operate, how their performance in this regard might be measured and whether special arrangements were required for sensitive sites. The results were presented at the World Parks Congress in Durban, South Africa in the autumn of 2003.

This preparatory work, as well as consultation with companies and experts, enabled us to develop a framework to use to benchmark companies' governance structures, policy and strategy, their management and implementation of those policies and strategies, and the quality of their assurance and reporting.

<sup>1</sup> 'Biological diversity', or biodiversity, refers to the variability among all living organisms and the ecological complexes of which they are part; this includes diversity within species, between species and of ecosystems.

## The benchmarking process

We determined that biodiversity risk was relevant to 22 companies in which we had shareholdings at the end of 2003. We first established an initial score for these companies by assessing their published materials and information generated through our previous discussions with them. Then, in January 2004, each company was invited to review its provisional benchmark score, and our analysis, to ensure this was an accurate reflection of its activities. The companies were also offered the opportunity to supplement their public disclosure with additional internal information, if they wished. Sixteen companies did so.

## The results of the first benchmark and subsequent engagement

Overall, companies' processes to ensure that their policy commitments were implemented appeared to be in their infancy, and varied considerably between and within sectors. A number of companies had some processes in place to manage biodiversity-related risks and opportunities, and many more were aware of the issues and mobilising resources to address the issue. Over half of the companies had some form of business-wide policy or strategy in place, but, for the large part, these lacked the detail required to provide a robust framework to drive improvement in performance across the business and to assure the effective management of biodiversity risks and impacts.

We then contacted each of the companies to suggest a range of specific steps (typically, between six to fifteen specific measures for each company) we felt each could take, depending on its risk exposure, to be confident that it was operating according to best practice.

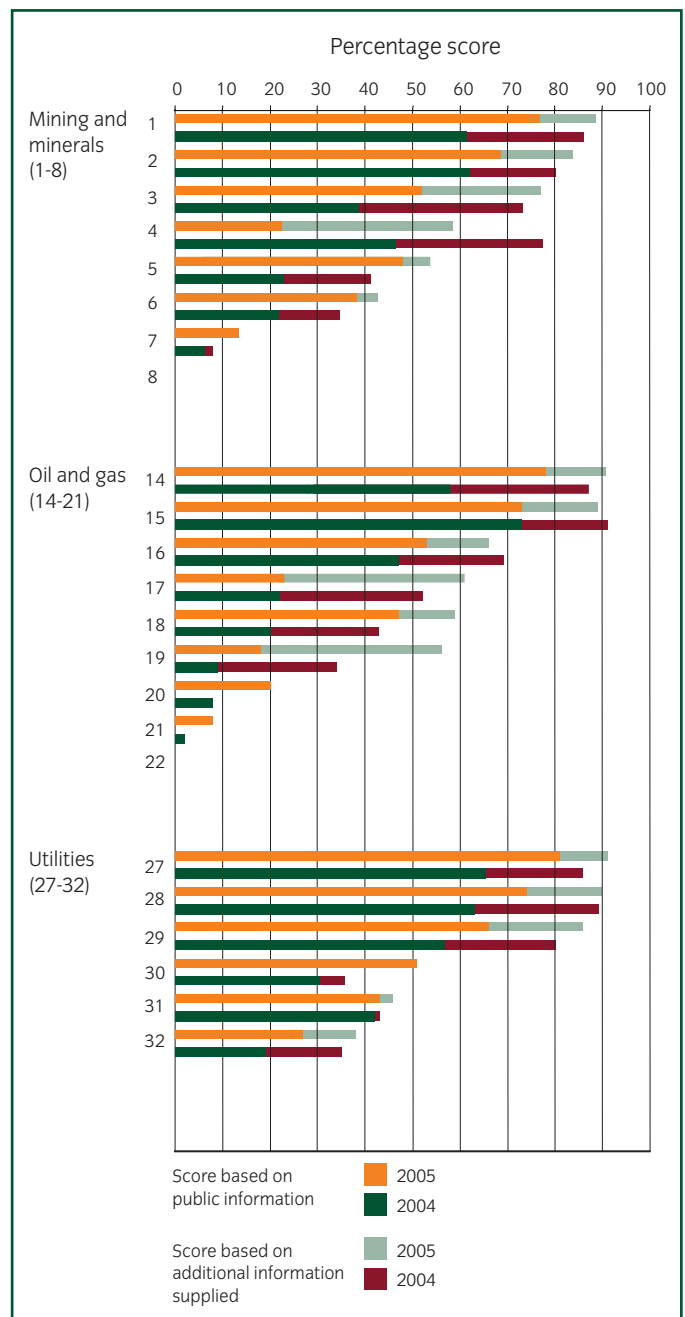
## The second benchmark

A year later, in 2005, we repeated the benchmark to assess whether any of the companies had implemented any or our recommendations, or otherwise made improvements to the way they manage biodiversity risks. For the second exercise, we collaborated with Fauna and Flora International (FFI), the world's longest established and well respected international conservation group. We also collaborated with the Dutch Social Investors' Forum (VBDO) and the Netherlands Ministry of Housing, Spatial Planning and the Environment (VROM). Funding from these agencies enabled us to assess a larger number of companies and extend our analysis to include additional issues. (Several of the companies benchmarked in 2004 asked us to include more companies in a second

benchmark, enabling them to compare their performance against a wider peer group. We added 14 companies to the universe analysed, increasing the total number of companies evaluated to 36.)

Companies were assessed against the same criteria as in the original benchmark, so as to be able to judge their progress and aid comparison. In addition, we added eight criteria aimed at evaluating companies' leadership in this area. (Companies were given their scores for this new section, but they were zero-weighted in the final results so companies could compare their results in 2005 on the same footing as those in 2004.) Again, research was initially based on publicly-available information and supplemented with additional data that 20 of the 36 companies chose to provide.

Figure 1: Benchmark results for 2004 and 2005



## The results of the second benchmark: what do they tell us about the effectiveness of engagement ?

The performance of the vast majority (86%) of companies has improved since 2004. The overall trend for improvement is evident from Figure 1, which shows the scores from 2004 and 2005. The increase in average score for each sector is shown in Figure 2:

Figure 2: Improvement in companies' performance

Sector	2004	2005	Increase
Oil and Gas	48%	56%	8%
Mining	46%	51%	5%
Utilities	62%	66%	4%

Five companies (Cairn Energy, Xstrata, Venture, Soco and Tullow) more than doubled their performance from the previous benchmark, although Soco and Tullow's scores started from a low base.

These results show that a number of companies have made great strides in developing processes to manage biodiversity-related risks and opportunities and in their communication of the issue; others are starting to tackle it in a systematic manner. Clearly, several companies have a considerable way to go before they can be confident that they are managing biodiversity risk according to best practice. Just as in 2004, we have used the results of the benchmark to engage with each of them individually, specifically recommending the steps each could take

to improve their management of biodiversity issues. Based on our experience of the improvements made by companies since the last benchmark, we have every confidence that the engagement will be equally effective this time.

## Conclusion

Insight is convinced that properly planned engagement by investors, using rigorous and effective analytical tools, can deliver substantial, demonstrable improvements in companies' governance and management of key social, ethical and environmental issues.

Benchmarking, based on careful research and engagement, helps companies, government and investors to identify leaders and laggards in the sector or sectors being evaluated, to identify companies' specific strengths and weaknesses on a particular issue and to highlight the improvements that companies have made over specific time frames. Moreover, it helps to clarify best practice and make clear to companies what investors expect of them on particular issues.

Clearly, Insight's engagement is not the only factor at work here. Other organisations are also working to encourage companies to address biodiversity issues more effectively, including some governments and several NGOs. Nevertheless, most companies have greatly improved their management and reporting of many of the issues addressed in the 2005 benchmark, in line with the suggestions we made to them in 2004. We are therefore confident that our engagement, and the benchmarking process specifically, was a major factor in driving companies to make these changes.

## Produced by the Insight Investor Responsibility Team

Web: [http://www.insightinvestment.com/responsibility/investor\\_responsibility\\_home.asp](http://www.insightinvestment.com/responsibility/investor_responsibility_home.asp)

Tel: 020 7321 1162