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DISCUSSION-OPINION-EDITORIAL™

What makes the board of directors of a mining company with ESG mandate

Major mining disasters of the recent times must not be ignored. Take the dam disaster in Brazil. The Brumadinhodam of Vale contained waste from an iron ore mine but gave way, unleashing a sea of mud which engulfed a staff canteen, offices and farms. Senior staff at the company responsible - Brazilian mining giant Vale - are facing murder charges over the January 2019 disaster. The move seals Vale's aim to "fully compensate" for the disaster, it said. Communities hit by a dam disaster in Brazil two years ago which killed 270 people will get a \$7bn (£5bn) payout. The state government said the amount was an initial estimate and that the company would have to pay more if necessary. "The agreement requires Vale to fully repair all environmental damage. The above-mentioned amount... could be increased if necessary," it said in a statement.Vale said it would pay both "socio-economic" and "socio-environmental" reparations, funding projects to repair the surrounding environment, including a massive clean-up of the Paraopeba river. The loss of life and reputation and the staggering burden of shame and guilt do not bode well for the company. After the 2019 Brumadinho disaster, Brazilian prosecutors charged 16 people, including Vale's ex-president Fabio Schvartsman, with intentional homicide and environmental offences, alleging they hid the risk of a dam collapse. This is where the company board's involvement come in the picture.

The board of a mining company assumes a lot of power and they have the guidance role of the CEO. The CEO-board relationship is defined by roles that differ from, but depend on, each other. A CEO is in charge of developing and executing strategy, while the board is responsible for approving and advising CEO on it. Day-to-day operations are the responsibility of the CEO, with the board providing a broader boundaries and perspective.

ESG

Environmental, Social, and Corporate Governance (ESG) is an evaluation of a firm's collective conscientiousness for social and environmental factors. It is typically a score that is compiled from data collected surrounding specific metrics related to intangible assets within the enterprise. It could be considered a form of corporate social credit score. Research shows that such intangible assets comprise an increasing percentage of future enterprise value. While there are many ways to think of intangible asset metrics, these three central factors together, ESG. They are used for a myriad of specific purposes with the ultimate objective of measuring elements related to sustainability and societal impact of a company or business. MSCI, a global ESG Rating agency uses the term from investment perspective and defines ESG investing as the consideration of environmental, social and governance factors alongside financial factors in the investment decision-making process. Standard & Poor's (S&P) highlights that through ESG investing, market participants consider in their decision-making the ways in which environmental, social, and governance (ESG) risks and opportunities can have material impacts on companies' performance. Investors who use ESG in their

Fig.1: The muddy sludge of the tailing dam buried the dam's cafeteria where hundreds of workers were eating (reference and image courtesy:https://www.bbc.com/news/business-55924743)

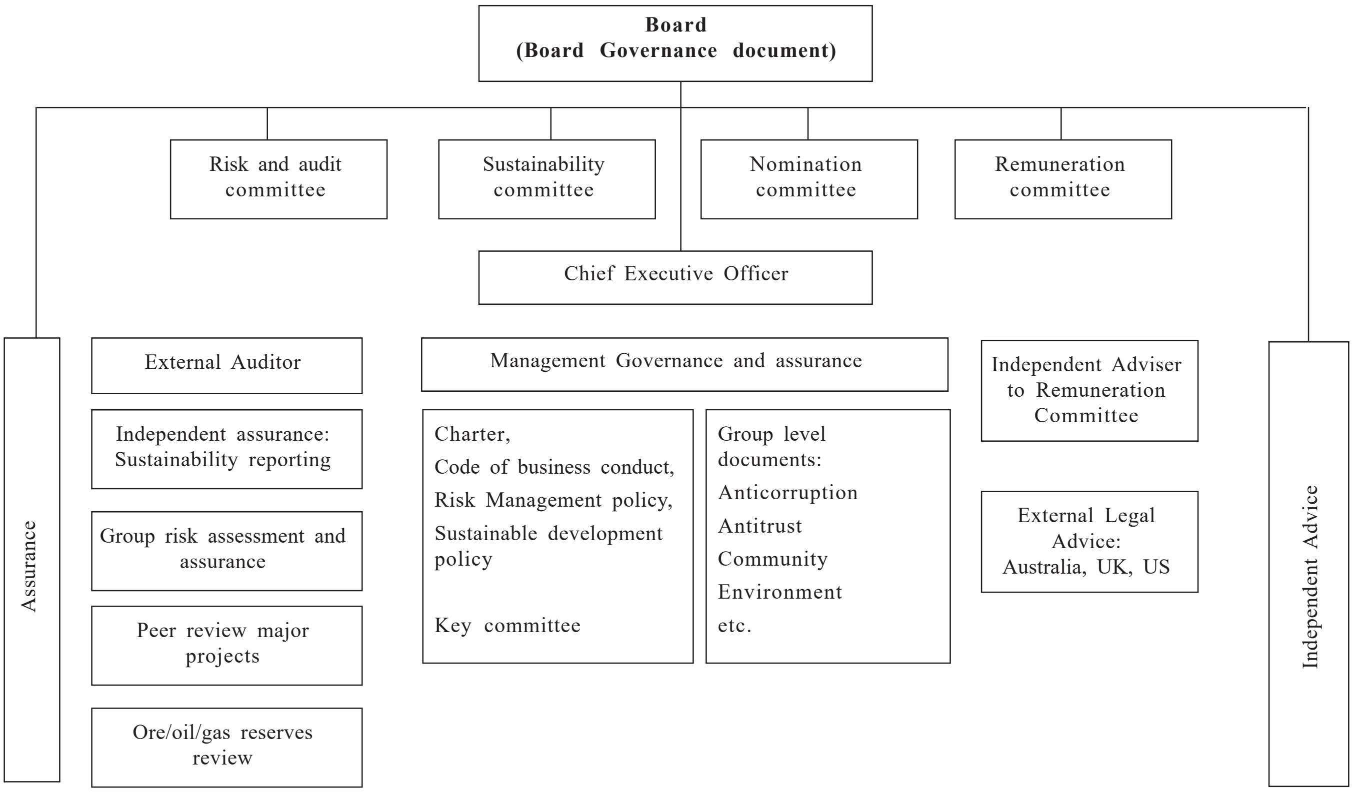


Fig.2: BHP billiton governance structure

(courtesy: https://www.researchgate.net/publication/312114239_Qualitative_Content_Analysis_Results_and_Discussion/figures?lo=1)

decision-making are able to invest sustainably while maintaining the same level of financial returns as they would with a standard investment approach.

ESG – environmental, social and governance – and the issues it embraces are notnew to the mining industry though the term may sound unfamiliar. Miners are constantly castigated with matters related to the 'green' or sustainability agenda, but ESG now brings together all these themes in a comprehensive framework that can help a mining company navigate and balance the benefits to the planet, people and profit successfully and emphatically.

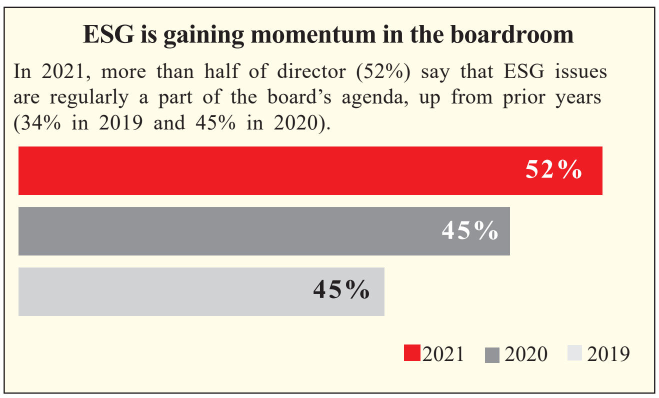
ESG has come to the fore primarily through investors demanding increased attention on environmental, social and governance-related matters and data. In short, investors are starting to look beyond financial statements and now want to consider the ethics, competitive advantage and culture of a mining organization. They have been proposing new standards and frameworks against which mining investments should be measured.

Against this background, mining companies should take a stewardship role rather than the ones looking for cover and excuse to navigate the ESG agenda for the industry:

- Environment: biodiversity, ecosystem services, water management, mine waste/tailings, air, noise, energy, climate change (carbon footprint, greenhouse gas), hazardous substances, mine closure.
- Social: human rights, land use, resettlement, vulnerable people, gender, labour practices, worker/community health and safety, security, artisanal miners, mine closure/after use.
- Governance: legal compliance, ethics, anti-bribery and corruption (ABC), transparency.

ESG mandate

Environmental, social and governance (ESG) issues are increasingly seen by public and private shareholders as a window into the future. And a clear hierarchy is emerging. Leading companies view ESG issues as a business imperative.



(Source: https://www.pwc.com/us/en/services/governance-insights-center/library/esg-corporate-directors-guide.html)
Courtesy: Earnest & Young

	1	2	3
Primary force	**Exponential climate impacts**	**Gen Z rising**	**Powering human augmentation**
Descrip-tion	**The world is now entering a new phase of climate change marked by exponential climate impacts,** volatility and related economic and social disruption.	**The next decade will be shaped by the naturation of Generation Z.** whose cohorts are generally more progressive on social issues than preceding generations and share a commitment to global sustainability.	**We are on the cusp of a revolution powered by human augmentation technologies** – Al, autonomous vehicles, robots, augmented and virtual reality and more.
Business Impact	**Climate impacts threaten more than supply chalns and physical infrastructure** – they endanger growth by exacerbating systems level disruption to customers, investors, employees and communities.	**As consumers, investors and employees, Gen Z will likely bring different expectations** related to sustainability, society, technology and ethics, and the role of private com panies in providing public goods.	**These accelerating technological disruptions simultaneously uncover opportunities** for more strategic and creative work and raise questions about the training and broader economic security of the workforce.

Courtesy: Earnest & Young

They manage risks while capitalizing on opportunities, including sharing their story and vision for the future, setting themselves up for long-term success and value creation in the process. Laggards still think of ESG as a check-the-box exercise grounded in only philanthropic activities. A company's ESG strategy spans a wide swath of the organization, requiring multiple functions to work together towards common goals and aligning that tie deeply and directly to the overall business strategy. Oversight from the board is becoming essential in crafting a compelling ESG story and bringing it to life.

What the boards should look for

Board checkbox

Strategy and alignment: Are ESG risks and opportunities integrated into the company's long-term strategy? How is the company measuring and monitoring its progress against milestones and goals set as part of the strategy?

Saying it loud and clear: Do ESG messaging and activities align with the company's purpose and stakeholder interests?

Failure risk assessment: Have material ESG risks been identified and incorporated into the enterprise resource management? For example, having a well-managed dam may cost the company $1 billion but its catastrophic failure will cost a minimum of $10 billion dollars in damages and loss of opportunities and goodwill. Has the board allocated the oversight of these risks to the full board or individual committees?

Strategic reporting: What is the best communication platform to use for the company's ESG disclosures? Do they need to be responsive to the media manipulations and what are the legal contexts?

Accounting: Do the ESG actions bring benefit to the company. What is the cost-benefit analysis?

Auditing

Disclosures: Are the ESG disclosures (both qualitative and quantitative) investor grade? Which ESG frameworks and/or standards is the company using?

Processes and controls: Are there processes and controls in place to ensure ESG disclosures are accurate, comparable, and consistent?

Assurance: Should independent and responsible assurance be obtained to ensure ESG disclosures are reliable?

Compensation for Responsibility

Accountability: Are the ESG goals and milestones effectively integrated into executive compensation plans?

Talent and culture: How is management organized to execute the ESG strategy? Are the right people and processes in place? Does the company have a culture which embraces ESG efforts?

Preparedness

Engagement: Is the company's ESG story being effectively communicated to investors and other stakeholders? Is it showing any response in the investment market?

Board composition: Does the board have the necessary expertise and skills to oversee ESG risks and opportunities?

Education and exposure: Does the board understand why ESG is important to investors and other stakeholders? Is the board appropriately educated and immersive in thinking on ESG?

Why Boards Fail

Were the directors asleep at the wheel? In cahoots with corrupt management teams? Simply incompetent? It seems inconceivable that lack of oversight disasters of such magnitude could happen without gross or even criminal negligence on the part of board members. When the directors are compensated for their roles why cannot they fail to do the job when needed. And yet a close examination of those boards reveals no broad pattern of incompetence or corruption. In fact, the boards followed most of the accepted standards for board operations: Members showed up for meetings; they had lots of personal interest involved or money invested in the company; audit committees, compensation committees, and codes of ethics were in place; the boards were not actually too small, too big, too old, or too young. Finally, while some companies have had problems with director independence because of the number of insiders (family members and friends of the owners) on their boards, this was not true of all the failed boards, and board makeup was generally the same for companies with failed boards and those with well-managed ones.

What really matters?

Attendance matters?

Regular meeting attendance is considered a hallmark of the conscientious director. It matters a lot and, still, a post failure dialogue often says, "Some big names on the boards…barely show up due to other commitments, and when they show, they're not prepared."Good attendance is important for individual board members, but it alone does not seem to have much impact on whether the boards are successful.

Helping mining companies communicate risks and stakeholder engagement practices

Building ESG into the investment case it is a key differentiator for you

(Figure courtesy: https://buchanan.uk.com/2020/02/14/esg-investment-case/)

Equity Involvement

Board members are assumed to be more vigilant if they hold big chunks of the company's stock—but data from the Corporate Library do not suggest that this measure by itself separates good boards from bad.

Board Member Skills

It is certainly true that many board members have their jobs because they're famous, rich, well connected—anything but financially literate. But just as many board members have the training and smarts to detect problems and somehow they can still fail to do their jobs anyway.

Board Member Age

There is a general belief that boards become less effective as the average age of their members rises-but not necessarily so. Age is often an asset, desirable but not entirely essential.

The Past CEO in the board: elephant in the room?

The situation is complicated: sometimes a past CEO's presence is helpful and sometimes it is not. There is regularly vilification that the "old dragons" who haunt successors by serving on boards. In certain cases, this can be a problem but can be a part of the solution as well. Alternately, a retired CEO can play an invaluable internal role as a mentor, sounding board, and link to critical outside parties.

Independence

Good-governance advocates and stock exchange heavyweights alike have argued that boards with too many insiders are less clean and less accountable.

Board size and committees

What is the right board size? Small is considered inadequate, big is considered bad. But both are pretty common.

Another area where good companies sticks to are executive sessions, which give boards the chance to evaluate their CEOs without interference. Executive sessions are also sometimes coupled with a designated lead director. Another supposed safeguard of good governance – audit and compensation committees – turns out to be near universal.

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