

C O M M E N T

More Walk, Less Talk: Comment on *How Cheap Is Corporate Talk?*

by Alan Horowitz

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Life in a public company can, at times, feel schizophrenic. Capital investments compete with cash flow targets; stretch performance goals compete with personal development and wellness initiatives; and short-term profitability expectations compete with long-term value creation opportunities. Perhaps not surprisingly, these tensions often manifest into wicked challenges and, at times, contradictions: Ambitious public financial, social, and environmental targets belie the nervousness and uncertainty that dominate board room discussions. A CEO's morning email to staff sounds curiously different from the answer to an analyst's "difficult" question during a quarterly earnings call. And yes, company statements in SEC 10-K filings about the potential implications of emerging public policy developments can sound quite different than contemporaneous comments on proposed rulemaking. Surprising? No. Resolvable? Perhaps.

James Coleman's illumination of one specific manifestation of this corporate dilemma—the "two audience problem"—is timely and important. Using the notice and comment process behind the Renewable Fuel Standard as his data source, Coleman observes that public companies can on the one hand raise fierce objection and even doomsday-like concerns during the rulemaking process yet remain sanguine in the context of SEC securities filings. Similarly, companies may convert a rule with modest—and even uncertain—upsides into compelling statements of long-term opportunity for investors. His conclusion, using carefully coded data comparing rulemaking comments with contemporaneous SEC documents, is that the truth is at best hard to discern and at worst, masked by "cheap talk" and even bad faith.

Yet, what Coleman exposes is more a manifestation of organizational complexity and conflict than rampant misdirection or duplicity. In fact, instead of relying exclusively on the presence of inconsistency between SEC filings and rulemaking submissions to gauge the credibility and trustworthiness of public companies, we should look more deeply into the way a company recognizes, navigates, and reconciles these natural organizational tensions. Reputable companies make decisions in a transparent and principled

manner, informed by the entity's core purpose, values, and long-term strategy. They are guided by authentic leaders who acknowledge complexity and reduce it to its simplest forms. They are governed by formal structures and informal networks that tackle these issues openly and constructively. And they recognize that their ability to create long-term value will be dictated by the company's willingness to balance and reconcile business growth opportunities with the needs of society and the limitations of our planet. Simply put, legitimate questions arise when these internal business management conflicts spill into the public domain, and it is incumbent upon companies who want to effectively engage in the policymaking process to resolve the sources of these discrepancies.

In a very recent study that in some ways parallels Coleman's work, the World Business Council for Sustainable Development (WBCSD) examines the frequent disconnect between company sustainability reports and risk statements in their Annual Reports.¹ WBCSD identifies several factors behind what it calls the "breakdown" in sustainability risk management, including: limited knowledge of sustainability risks within companies, longer time horizons for sustainability risks, and differing purposes for sustainability compared to risk disclosures. Some of these challenges or hurdles can be extrapolated to the "two audience" problem exposed by Coleman and could offer a roadmap for mitigation, if not resolution.

(1) The Organization Hurdle: Much of the complexity that is found in large public companies is associated with their size, their organizational structures and, to be sure, the big, and often competing, personalities, perspectives, and ambitions of their people. For example, Environmental, Health & Safety technical professionals tasked with evaluating the costs and benefits of proposed rules are disconnected from the Corporate Secretary and Investor Relations teams. Lawyers drafting the comments do not coordinate their work with their colleagues in the

1. WORLD BUSINESS COUNCIL FOR SUSTAINABLE DEVELOPMENT, SUSTAINABILITY AND ENTERPRISE RISK MANAGEMENT: THE FIRST STEP TOWARDS INTEGRATION (2017), available at <http://www.wbcd.org/Projects/Non-financial-Measurement-and-Valuation/Resources/Sustainability-and-enterprise-risk-management-The-first-step-towards-integration>.

Corporate Secretary's office. These disjointed teams don't understand each other's language, speak to vastly different internal and external audiences, and use different and even conflicting risk assessment and management tools. These dynamics have practical and even embarrassing consequences when perspectives are not shared, individuals are uninformed, and teams lack joined-up perspectives. This hurdle can be overcome through better governance, stronger internal networks, and a stronger appreciation that the company's credibility may depend on improved coordination, alignment and collaboration.

(2) The Purpose Hurdle: In the context of a rulemaking initiative, a company is an advocate, looking to promote its interests and, presumably, what it considers sound public policy. The language of the proposed rule is parsed, cost-benefit analysis is performed, and positions are taken. In contrast, the SEC filing process is about assessing and communicating company "risk factors," defining what is or is not "material" (an endless debate), and otherwise searching for the level of transparency required by law and demanded by investors. Consequently, the processes are managed with disparate, if not conflicting, lenses in the context of different legal frameworks and for vastly different audiences. The consequence, as Coleman shows, is an opaque, if not obscure, window on a company's analysis, perspectives, and policy positions.

Change will arise when investors demand, or regulators compel, greater transparency on how companies view longer-term environmental and social threats and opportunities. This transformation is beginning: Sustainable Accounting Standards Board (SASB) disclosure standards are being developed; institutional investors are showing ever-increasing interest in the "Environmental, Societal and Governance" performance of organizations; and companies are making strategic shifts that recognize—whether they believe it or not—the interconnection between their growth prospects and a changing planet. In these ways, the bridges between traditional disclosures of quantifiable

financial risks and more qualitative "sustainability" risks are being built and the communication gaps exposed by Coleman should, over time, subside.

(3) The Leadership Hurdle: As feckless politicians and disaffected electorates turn their nation states inward, the world increasingly needs civil society and the private sector to fill the void. CEOs must build cultures and drive incentives that promote a more holistic sense of corporate responsibility, driving toward delivery of the UN Sustainable Development Goals. CFOs must back public commitments to environmental protection with capital investments. And General Counsel must ensure that forward-looking statements of risks in SEC filings are not contradicted by responses to proposed rulemaking, lobbying efforts or other public actions taken to promote shorter-term challenges. In other words, companies need leaders who create cultures where "doing the right thing" for the long-term health of the company, society and the planet is valued, demanded and rewarded. Those companies are much less likely to suffer from the form of corporate schizophrenia that Coleman illuminates.

Coleman's core prescriptions for improvement—advising regulators to compare comments with securities disclosures; counseling plaintiff's lawyers to audit SEC filings for accuracy and completeness; and encouraging corporate counsel to drive alignment between comments and disclosures—are sensible. Yet, they largely address the symptoms of the behavior, not the underlying causes. More effective, and predictable, alignment across public filings; greater trust in institutions; and more sustainable public policy will be achieved when companies are able and willing to acknowledge, address, and surmount their "organization," "purpose" and "leadership" hurdles. Those that fail to do so will continue to put both their short-term reputation and prospects at risk. Those that do will turn their "cheap talk" into a valued and trusted voice of reason. These are the companies that will be around for the long term, and deservedly so!