

HEIDRICK & STRUGGLES

The emergence of the
Chief Sustainability Officer

From Compliance Manager to Business Partner

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Overview

In the past twelve months our firm has witnessed a substantial rise in demand for a new breed of environmental, health, and safety (EHS) leader – now often known as the Chief Sustainability Officer (CSO), to mark the transformation of the role. While technical skills are important, companies today hunger for leaders who think strategically, communicate clearly and persuasively, and possess sound business knowledge and judgment – people with broad vision and creativity. Increasingly, the companies we work with and the experts we talk to say that a successful CSO – like the successful CFO or Chief Marketing Officer – needs to think and act like a CEO.

No longer merely an audit and compliance manager, this new breed of corporate leader works directly with other top corporate leaders, frames EHS issues in strategic terms, and operates in the far broader context of environmental and social sustainability.

To help companies take advantage of these rapidly evolving trends, this white paper:

- Details the pressures driving this demand as well as the benefits – from enhanced brand and reputation to reduced costs, increased efficiency and competitive advantage – this new breed of leader can provide.
- Identifies the most pressing EHS issues on the horizon, including climate change, materials of concern, the environmental impact of India and China, energy costs, technology development and more.
- Profiles the broad new arsenal of capabilities that today's Chief Sustainability Officer needs, including ability to convert challenges to opportunities, translate technical issues into compelling communications to all stakeholders, engage the full range of sustainability challenges, put financial understanding to work, and maintain a global perspective.

Understanding the new demands of this role and finding the right people to fill it should be a high priority for companies that want to maintain public confidence and protect shareholder value – especially those in industries with high EHS risks. Drawing on in-depth interviews with experts on three continents and our executive search experience, “The Emergence of the Chief Sustainability Officer: From Compliance Manager to Business Partner” presents a picture of the EHS role in transition and offers some valuable recommendations about finding the right people to fill this increasingly vital position.



An evolving role worldwide

In North America, Europe, and much of the Asia-Pacific region, the days are gone when the chief EHS leader worried only about audit and compliance and interacted mainly with permit writers, safety inspectors, and low-level compliance staff at regulatory agencies. Today, because the stakes for a company are so high – and getting higher – CSOs now deal directly with senior personnel at regulatory agencies. They also serve on a number of senior-level advisory groups and associations aimed at influencing public policy developments and regulations or dealing proactively with specific challenges to their particular industry or value chain as a whole. In many cases, they have significant responsibility for delivering on key business objectives such as a company's profitability and growth and helping maintain shareholder value.

"I've seen the role change from a tactical, day-to-day compliance role that served within the General Counsel or HR function to a strategic role that often has significant responsibility for the growth and performance of a company, interacting regularly with the CEO, COO, CFO, and board members," says Allan Bedwell, principal with Camp Dresser McKee Inc, an environmental engineering, consulting, and construction management firm, providing full environmental services to industry and government.

As head of Environment, Health, Safety and Sustainability at Santos, a major Australian oil and gas company with interests in Asia Pacific, the US, and the Middle East, Andrew Antony manages multiple relationships throughout the organisation. "I have regular interaction with the CEO, the Board sub-committee, the VPs – including operations, development projects and ventures into new countries, and the operations management group," he says. "While many companies combine health, safety and environment, we've taken the next step and included sustainability. The portfolio has common elements – they all require good systems, sound strategies, and audit and monitoring programmes. And sustainability is about getting a balance across all the competing drivers and achieving value."

Like Santos, Akzo Nobel NV, the global animal healthcare products, coatings, and chemicals company, has also expanded EHS to include sustainability as well as corporate social responsibility (CSR). In 2003, the company created the role of Director, Corporate Social Responsibility, Health, Safety, and Environment and appointed Andre Veneman, who serves in the role

today. He reports directly to the company's CEO and is responsible for ensuring that EHS remains high on the corporate agenda. The company also has a Corporate Social Responsibility Council, which includes Veneman, the CEO, two of the company's ten business unit managers, the Chief Technology Officer, Chief Strategy Officer, Director of Human Resources, Director of Communications, and the Marketing Manager. Meeting three times yearly, the Council sets CSR and EHS policy. In addition, Akzo has some 200 EHS managers worldwide to ensure that CSR and EHS are cascaded down the organisation.

Wim Jetten, Director of EH&S for Dow Chemical Europe, says that the upgrading of the EHS role has gone hand in hand with the broadening of EHS to encompass CSR and sustainability. His company's approach has expanded from programmes and management systems designed to meet company and government standards to programmes proactively concerned with the public good. Dow's long-term plans now encompass not only addressing accidents, incidents, and carbon emissions, but also addressing essential human issues such as the lack of clean drinking water in developing countries by developing technologies to help solve the problem. "We realise that our future as a company," he says, "depends on the future of other people and our impact on the environment and natural resources."

Pressures to change

The increased prominence of EHS and sustainability was initially driven in response to aggressive governmental enforcement in the US and, more recently, in the European Union (EU). Regulations proliferated and violations were often punished with heavy fines; and there are no signs this will change.

"The stringency of regulation, both domestically and internationally, continues to increase as the complex relationship between emissions, discharges, product materials, waste handling, and environmental and health impacts are further understood by the scientific community," says Bedwell. "At the same time, regulatory agencies and case law are not waiting for the scientific evidence. In some cases public reaction, media frenzy, or political agendas are driving new regulations."

EHS and sustainability performance continues to come under increasing scrutiny from a variety of perspectives and sources, including:

Financial

Over the past several years an increasing number of rating agencies and financial analysts have identified environmental and safety performance as an evaluation metric.

“EHS is increasingly viewed as a material risk for companies from the standpoint of investors, insurers, lenders and rating agencies,” says Bedwell. “Companies with significant liability or poor performance are viewed as higher risk investments or as investments with poorer ROI.” He cites the example of two prominent utilities. Utility A had effectively managed its liabilities and, as a result, was rated as a good investment. Utility B, which had significant waste and air pollution problems, had negative ratings and in fact was passed by for acquisition several times over a nine-year period.

Legal

Environmental organisations, non-government organisations (NGOs), and regulatory agencies have undertaken litigation against many companies, adversely affecting their operations and financial performance. Class-action lawsuits filed by third parties over worker or community health issues from products or operations are also sharply on the rise.

“Two areas of legal liability that have dramatically increased for companies in the last ten years are environmental justice and natural resources damage,” says Bedwell. “Environmental justice is perceived or actual disproportionate impacts to economically disadvantaged or minority communities. Natural resources damage is liability for impacts to natural resources. Government agencies and courts have been increasingly promulgating regulations or deciding in favour of environmental justice or natural resource impacts.”

Large settlements, fines, and the cost of changing processes, altering products, and undertaking environmental remediation can, of course, significantly affect financial performance and, in extreme cases, put the survival of the company at risk.

Public interest

Community, environmental, and other public interest organisations and advocacy groups have become increasingly adept at challenging companies on EHS and sustainability issues, lobbying policy makers, and mounting public campaigns against perceived malefactors.

Moreover, using the Internet’s dizzying variety of websites, newsgroups, and blogs, these organisations – or even a sufficiently zealous individual – can directly affect the stock price of targeted companies by mobilising enormous numbers of people to pressure institutional investors to boycott or dump a stock, a tactic that can be more effective than product boycotts.

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Sourcing

Many business customers now require their suppliers to participate in sustainable sourcing and will not source from companies that aren't ISO 14001 certified. They are also likely to opt for suppliers who can show they have developed a strong platform in EHS for their own business.

Media

In an age of 24-hour news, a wired world, and more information sources than ever, media attention can turn a problem into a crisis almost overnight.

In response to the initial wave of regulation, many companies adopted a compliance-at-any-cost stance that led to bloated auditing budgets, enormous investments of time and resources, and ballooning costs. In a time of increasing cost pressure, however, such an approach is not sustainable.

Positive incentive to change

“Companies now are looking to reduce their costs of maintaining and documenting compliance, especially with auditing programmes that catch errors after they've happened and often consume inordinate management resources for the correction of fairly trivial issues,” says John Blatz, a leading EHS consultant and former Senior Vice President of Environmental Health and Safety at Great Lakes Chemical Corporation. “Instead,

they increasingly focus on continual improvement of integrated management systems in place of the 'find and fix' mentality of most audit programmes.”

In adopting more sophisticated approaches to EHS and sustainability, many companies have discovered a surprising number of substantial business benefits, including:

Enhanced brand

Within the past five years, the environmental and safety implications of products and company performance have caught the attention of the media and consumers. Many consumers are increasingly basing their purchasing decisions, at least in part, on EHS and sustainability. So are large organisations. The mayor of New York City recently announced his determination to replace the city's entire taxi fleet with hybrid vehicles.

Preservation and enhancement of reputation

Outstanding EHS performance not only enhances a company's reputation with external stakeholders but also with employees, who take pride in that reputation. According to Andrew Antony an increasing number of graduates at job interviews are asking questions about their prospective employers' sustainability, water quality, and climate change policies. “We don't have figures yet on how this affects their choice of employer, but if you're publicly seen as not managing these issues well, you would expect it to be a deterrent to attracting talent,” he says.

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Decreased costs

“Well planned, communicated, and executed initiatives can make all the difference in reducing risks and incidents,” says the VP of EHS of a large industrial company. “This could lead to lower insurance payments, less operational costs, lower workers’ compensation costs, avoidance of non-compliance and associated fines, and more. That is how you make the biggest impact on any company – reducing costs.”

Protection of assets

Beyond simply preserving financial assets from claims and penalties, superior EHS performance can also help preserve physical assets by precluding the fires, explosions, and other accidents that can shut down plants.

Increased efficiency

It has been shown that safe, environmentally sound operations are also more efficient, perhaps as a result of the conscious scrutiny of processes that good EHS practices require. In fact, such gains in efficiency can help offset the costs of compliance.

Competitive advantage

By achieving best-in-class total cost of EHS risk management, companies can gain such competitive advantages as lower costs and the ability to enter new markets quickly without compliance problems. “For Santos it’s about operational excellence,” says Andrew Antony. “No incidents, no downtime, good productivity, good morale, and meeting regulator and community expectations.”

In addition to these pressures and incentives to change, say our experts, companies will face a new set of issues that will only intensify the need to adopt a more strategic approach to EHS and sustainability.

The gathering storm

Looking out over the next five years, our experts agree that the most pressing issues will include:


Climate change

Global warming and regulations requiring cuts in carbon emissions will unquestionably pose the greatest environmental challenge for the foreseeable future. It is estimated that companies will be required to cut approximately 25% of carbon emissions by 2020 and 50 – 80% by 2050. In the US, eleven states have already adopted those carbon limits; another twenty states are expected to follow suit shortly. The European Union has set an ambitious goal of limiting global warming to no more than 2°C above the pre-industrial temperature. It already has in place a carbon capture and trade system that covers 45% of the continent’s emissions, 10,000 companies, and twenty-seven European Union countries – and the system is likely to expand its coverage in the future. In Australia the federal government recently announced that a carbon capture and trade system will be in place by 2012. In the next two to four years, the US government will likely establish greenhouse gas caps, too, while states continue to promulgate regulations that may be inconsistent with those of other states and the federal government. Further, countries around the world have established reduction targets and differing regulations.

“Almost any combustion source emits greenhouse gases, but the technology to reduce them will not be cost-effectively available until approximately 2050,” says Allan Bedwell. “The limits, however, take effect in 2020. That thirty year gap will create significant impacts for companies as they attempt to cost-effectively offset their regulations. The financial industry has identified this as the number one environmental material risk facing companies in the US and abroad.”

Materials of concern

On June 1, 2007, the European Union enacted a new chemical policy known as REACH, an acronym for the “Registration, Evaluation and Authorisation of Chemicals.” A substance rather than a product registration programme, REACH requires manufacturers and importers to register substances placed on the market in the EU above volumes of one metric ton per year. With some exceptions, it applies to all existing



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substances, including those listed on the European Inventory of Existing Commercial Chemical Substances (EINECS) and any new substances manufactured in the future.

REACH is an extremely ambitious chemical strategy, replacing forty existing EU laws and affecting multiple industries. Dow Chemical Europe’s Wim Jetten points out that Europe’s determination to be in the forefront on such issues may put some EU companies at a short-term cost disadvantage versus non-European competitors in markets outside the EU.

In the US, the Environmental Protection Agency (EPA), the Occupational Safety and Health Administration (OSHA), and other federal, state, and community regulators will continue to identify and regulate potentially harmful substances. Companies will be under pressure to reduce the use of these materials and find substitutes. They will also be expected to take responsibility for the harm to individuals, communities, and natural resources that such substances cause.

Environmental and social sustainability

Numerous guidelines and reporting standards for sustainability and social responsibility already exist, such as the Global Sullivan Standards and UN Global Compact, for evaluating performance in specific areas as well as CSR performance generally; and the Global Reporting Initiative (GRI), a reporting standard developed by CERES (Coalition for Environmentally Responsible Economies), an organisation encompassing corporations, non-governmental organisations, international organisations, United Nations agencies, business associations, universities, consultants, and accounting organisations. The drive for corporate social responsibility that these guidelines represent is likely to intensify – and become more all-encompassing.

“During the next five years, the definition will likely tighten and companies will not only need to ensure that its products are environmentally sustainable, but also ‘socially’ sustainable,” says Bedwell. “Companies with labour forces overseas will be held accountable for how those labourers are treated, their quality of life, and standard of living. This will put significant financial pressure on companies.”

Environmental impact of China and India

As the economies of China and India, representing a third of humanity, continue to grow, it is unclear whether they will adopt environmental standards as stringent as those in the West. If they do not, their domestic companies will gain a distinct cost advantage, and US and European companies may pay a disproportionate price for compliance. CSO's will be under increasing pressure to develop innovative solutions to offset these cost disadvantages.

Energy costs

Increased global energy demand, in part driven by the growth of China and India, will increase the worldwide demand for petroleum and natural gas, resulting in generally rising prices accompanied by unpredictable fluctuations in price. Carbon taxes and regulations designed to decrease greenhouse gas emissions will affect the availability and costs of energy, likely landing much of the energy challenges in the laps of the EHS leaders.

Technology development

Meeting environmental and regulatory challenges will require companies to develop, identify, and deploy new technologies and processes. "They will need to focus on engineering designs, technology, and applicability to reduce risks," says the VP of EHS of a major industrial company. "This is usually the last step for many reasons: it costs more, it is not as easy to understand and plan around, and you need to get very technical people involved at the front end of production."

The magnitude and multiplicity of these emerging issues, coupled with existing pressures, will require a new breed of EHS leader who can work creatively on many fronts at once, who enjoy confidence and trust at the highest levels of their companies, and who possess a broad and deep array of specific competencies.

The new breed

Today, in companies that understand the crucial role that EHS performance will increasingly play in overall company performance, the function is no longer

regarded as a cost centre but as a strategic asset, or, if poorly managed, a liability. In these companies, the CSO no longer reports into Legal or Human Resources, but directly to the CEO and interacts regularly with the CEO, President, CFO, other senior corporate leaders, and with board members. In this far more strategic role, the CSO frequently has significant responsibility for the growth and performance of the company.

Jim Schultz, the former Senior Vice President Employee and Customer Engagement at Waste Management observes, "In my experience, a solid EHS programme has to be genuine, and it has to be driven by a visionary leader who serves as the central 'change agent' and catalyst to drive employee engagement. This individual must be a visionary, a great communicator, and demonstrate enthusiasm. He or she must understand human nature and behaviour, and be a master facilitator. Optics are critical, and so the EHS leader must report directly to the top officer of the company."

If there is one overriding competency that the new-breed CSO will need in this new context, say our experts, is the ability to think strategically. This requires the ability to look toward the horizon, identify an opportunity or challenge before it affects the company, and develop and implement a strategy to either take advantage of the opportunity or manage the challenge. Dow Chemical Europe's Jetten says that EHS has moved not only from compliance management to sustainability management but also that sustainability should create business opportunities.

Akzo Nobel's Veneman provides a simple example of this convergence of EHS, sustainability, and business opportunity. The company has developed an anti-fouling marine coating that contains no toxic materials. The coating is so effective that it reduces fuel consumption on ships by 6%, a highly attractive proposition for the company's marine customers. And, because the shipping sector emits 4% of carbon in the world, the fuel savings translates into significant reductions in carbon emissions.

The new-breed CSO must also be able to communicate effectively, translating complex technical concepts and strategies into terms that resonate with the company's top leadership and key constituencies, including investors, lenders, insurers, rating agencies, customers, suppliers, the media and the public. Effective communication also requires considerable persuasive skill in dealing with everyone from the shop foreman to the CEO, board members, government regulators, policy makers, the press, and the public.

In addition to strategic and communication skills, the new world of EHS calls for a wide range of interdisciplinary and cross-functional competencies, including:

- Ability to hire, lead, develop, and inspire a diverse staff and to develop trusting relationships with a variety of company constituents before an issue becomes a problem.
- A solid grounding in a wide range of environmental, health and safety requirements, processes, procedures, technologies, and, depending upon the scope of the operation, familiarity with these issues at the local, state, federal, regional, and international levels.
- A knowledge of financial operations that extends beyond budgeting to include project financing, corporate finance, an understanding of how finance intersects with EHS and sustainability, and the ability to make a business case for a new direction.
- Knowledge of the company's processes, products, technologies and business processes coupled with the ability to manage environmental and safety systems within the company and the ability to assess and audit those systems with vendors, suppliers, and distributors.
- Familiarity with technological and process advances and an understanding of the trends in EHS and the influences on the company and the industry segment.
- Ability to communicate with community leaders and activists and to communicate with the media in a crisis.
- Ability to develop and manage a marketing campaign related to the EHS and sustainability aspects of the company's performance, products, or liability.

In short, it is far less important that the CSO knows the difference between a regenerative thermal oxidiser and a selective catalytic reduction system than it is to

possess the qualities of strategic orientation, business acumen, personal influence, and cross-functional competencies that characterise effective leaders.

“This role requires change agents,” says Andrew Antony. “You need the management skills required for any senior role, but applied to EHS it means the ability to establish and then implement a strategy, to introduce systems that effectively monitor and report, and the ability to manage, influence and lead people across the organisation.”

A number of pioneering companies, says Allan Bedwell, have found or developed such far-seeing, multi-talented leaders:

- Since the early 1990s, a specialty chemicals manufacturer, under the capable leadership of its Vice President of EHS, developed a “global issues management” approach to think creatively about what challenges were over the horizon and how the company could address them years before they became problems. The company also emphasised corporate stewardship and began a number of worldwide initiatives with other companies, including the World Business Council for Sustainable Development, the Global Environmental Management Initiative, and other organisations.
- Since 2003, a large, prominent paper manufacturer has produced a sustainability report and closely tracks its environmental, health, and safety performance. The company's Vice President for EHS has the strategic skills to get out in front of issues long before the rest of the industry is aware of them. He has built strong, trusting relationships with environmental and health organisations, which has helped enable the company to achieve a well-deserved reputation for superior environmental performance. Organisationally, he established a small, core EHS operation at headquarters, but decentralised the EHS operation, creating a partnership with plant managers to share accountability for performance of EHS functions.

“Effective CSO’s possess skills that far exceed those of officer. They have vision, strategic management ability, alliances, and communicate effectively both internally

- The Vice President of EHS for a large, publicly-owned utility, a low-key entrepreneur who has the full support and partnership of his CEO and board, has established the utility as one of the leading “green power companies.” Although the majority of the company’s power plants use fuel that is considered dirty, he has built a strong business case for going beyond regulatory requirements to minimise the company’s risk for decades to come. In the face of new greenhouse gas, fine particulate, and ozone regulations, his strategy has paid off. The company also owns the largest fleet of renewable energy assets in the US. The VP has also developed strong, long-lasting relationships with senior regulatory officials at the state and federal levels.

As these examples demonstrate, whether the EHS leader is with an automotive manufacturer, a mining company, an energy producer, a forest products company, a big-box retailer, or a financial services business, effective CSO’s possess skills that far exceed those of the traditional compliance officer. They have vision, strategic management ability, the ability to build diverse alliances, and communicate effectively both internally and externally. They quickly establish a track record of accomplishments that is unassailable and often serves as a model for other companies. They know how to hire, develop and inspire managers with vision, and they get results.

Finally, although EHS standards and regulations vary around the world, they are likely to continue to converge as well as expand everywhere to encompass sustainability. In this coming world, top CSO’s will bring a genuinely global perspective to challenges and opportunities that will only grow in importance to all of their companies’ stakeholders.

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