INTRODUCTION

A changing world brings with it new risks and opportunities for investors. Monitoring and analysing companies’ involvement in ESG controversies is an increasingly important part of the risk assessment process. It supports investors in understanding where gaps may exist between public ESG commitments, and operational practice. It can reveal where companies are exposed to reputational, operational and even legal risks that often sit outside the scope of traditional risk mapping activities. V.E have been building our controversy database since 2015 and to date, have over 20,000 cases logged and analysed across a broad range of ESG issues. In this 5 minute read, we provide a snapshot of our 2020 analysis. Many stakeholders have provided commentary on how social-risks have ‘come to the fore’ or ‘have been exposed’ as a result of the COVID-19 pandemic. This is clearly reflected in the high concentration of social controversies we captured in 2020. We are in the midst of a transition into an increasingly digitalised socio-economic environment that brings with it new and challenging risks for corporates and stakeholders. Unsurprisingly, we see software, technology and telecommunications companies amongst the most exposed to ESG controversies as regulators and civil society raise concerns on their operational activities. As ESG investing continues its rise, the scrutiny of the financial sectors (Diversified Banks, Insurance and General Financial services) remains high especially on issues such as Climate Change. In short, our findings appear to be a good reflection of the macro-trends that we see transforming the world today.

2020 TAKEAWAYS

- In 2020 we captured 3,655 new controversies impacting 1,413 companies.
- More than 50% of those controversies were linked to Social issues.
- We captured 328 COVID-19 related controversies impacting 235 companies.
- We saw a rise in climate-related controversies linked to continued shareholder activism and climate liability lawsuits.
- 35% of assessed companies provide no public response to the allegations that they face.
- The five most exposed sectors to controversies were Diversified Banks, Mining and Metals, Software and IT Services, Telecommunications and Technology and Hardware.
V.E FINDINGS

2020 Company Universe Covered by our Controversy Risk Assessment

Period under review
January 1, 2020 - December 31, 2020

Universe under review
7,938 Companies
39 Sectors

Companies monitored by region
North America: 3,423
Asia Pacific: 1,232
Europe: 1,986
Emerging Markets: 1,297

Percentage of Cases Overall

<table>
<thead>
<tr>
<th>Type of Controversy</th>
<th>Number of Cases Overall</th>
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<tr>
<td>E</td>
<td>662</td>
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<td>S</td>
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Top 10 Most Exposed Sectors

1) Diversified Banks
   376 Controversies Recorded
   11.8 % of Overall Controversies

2) Mining & Metals
   365
   11.4 %

3) Software & IT Services
   242
   7.6 %

4) Telecommunications
   167
   5.2 %

5) Technology Hardware
   153
   4.8 %

6) Food
   137
   4.3 %

7) Automobiles
   124
   3.9 %

8) Insurance
   124
   3.9 %

9) Specialised Retail
   118
   3.7 %

10) Financial Services - General
    113
    3.5 %

Top 10 Most Affected ESG Themes

1. Audit & Internal Controls
2. Customer Relations
3. Anti-Competitive Practices
4. Community Social Impact
5. Health & Safety
6. Climate Change
7. Fraud
8. Information to Customers
9. Water Pollution
10. Impact on Biodiversity
In 2020, the Diversified Banks sector faced a total of 376 controversies (a significant increase from 275 in 2019). The majority of these were Governance related (203 cases). 51% of the cases were of high severity.

Most of these were related to audit & internal controls (154 cases), money laundering (59 cases) and fraud (63 cases). With this high concentration of Governance controversies, the sector bucks the wider trend (with most other sectors facing predominantly environmental and social controversies). This indicates that structural efforts to strengthen ethical compliance systems are vital within the sector (as opposed to undertaking short term corrective actions as corruption controversies emerge). As ESG investing and sustainable finance continues to rise, the sector is face rising scrutiny with regards to the indirect impacts of their investment and lending activities.

We recorded a large number of controversies related to Climate Change (68 cases) and human rights violations (46 cases). The United Nations’ Responsible Banking Principles were launched in 2019 to help banks to align their strategies with the vision of society set out by the United Nations Sustainable Development Goals and the Paris Agreement. Over 2020 we saw signatories to the initiative grow by over 62% (from 132 in 2019 to 214 at the end of 2020). Signatories are committed to annual reporting and reviews. Looking ahead, it will be interesting to view what impact the initiative has on the overall ESG profile of signatory members and the sector overall.

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1 Within our methodology for assessing controversies, Severity is assessed on a 4 point scale: minor, significant, high, critical
2 Principles for Responsible Banking, UNEPFI Website, February 2021
In 2020, Mining & Metal companies faced a total of 365 allegations (a significant increase from 166 in 2019) The majority of these were social controversies. 47% of these were of high severity.

In line with our historical analysis, there continues to be a high concentration of cases related to negative community impacts (87 cases) and breaches of indigenous people’s rights (42 cases). Perhaps the most high-profile controversy within the sector in 2020 was related to indigenous rights with the Rio Tinto\(^3\) CEO eventually exiting the company following the destruction of two sacred Aboriginal sites by the company. The case helped to underscore the material impact that Human Rights controversies can have on corporates. From an environmental perspective, we continue to see a high volume of cases related to water pollution (67 cases) and biodiversity (59 cases). The 2019 Brumadinho dam collapse in Brazil\(^4\) saw implicated parties making billion-dollar payouts and has been followed by the launch of the Investor and Mining and Tailings Safety Initiative\(^5\). Now, we see rising investor interest on the topic of biodiversity (across several sectors). Given their high environmental footprint, we expect mining and metal companies to face more engagements from active investors on their environmental performance in the decade ahead.

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\(^3\) ‘Rio Tinto chief Sebastian Jacques to quit over aboriginal cave destruction’ — BBC News, 11/09/2020

\(^4\) ‘Brazil dam disaster: $7bn compensation for disaster victims’ — BBC News, 04/02/2019

\(^5\) ‘Investor Mining and Tailings Safety Initiative’ — Church of England website.
In 2020, Software & IT Services companies faced 242 allegations (a small increase from 236 in 2019). The majority of these were social controversies (171 cases). 33% of these were of high severity.

Most cases were linked to customer relations (61 cases) and privacy rights concerns (54 cases). Typically, these involved the reported collection of users’ private data without clear consent and/or the improper use of clients’ data for targeted advertisements. With COVID-19 shifting unprecedented number of workers into online working environments, concerns over data security and privacy will continue to be prominent in 2021. Software and IT companies are likely to face rising scrutiny from regulators as many nations look to position themselves to better manage the transition towards an increasingly digitalized economy. The sector is driving many profound changes in how our societies and economies function. Whilst this presents clear business opportunities for them, these companies will face challenges on multiple ESG fronts; cyberbullying, managing misinformation, tax payments, freedom of expression. With those dynamics in mind, it is perhaps not surprising to see that the fourth and fifth most exposed sectors to ESG controversies were Telecommunications and Technology and Hardware.
METHODOLOGY

V.E’s Controversy Risk Assessment screens 7700+ companies for their involvement in ESG controversies.

- All Controversies are systematically assessed in terms of their:
  - Severity: minor, significant, high, critical
  - Frequency: isolated, occasional, frequent, persistent
  - And the Responsiveness of the company: non-communicative, reactive, remediative, proactive

- Controversies are classified under a E-S-G taxonomy containing 38 themes:
  - Eg: Environment – Biodiversity, Water, Climate Change etc
  - Eg: Social – Child & Forced Labour, Non-Discrimination, Health and Safety etc
  - Eg: Governance – Executive Remuneration, Shareholders’ Rights etc

- Company records are updated on a daily basis:
  - Data files are refreshed daily
  - Individual company reports (PDFs) are refreshed daily
  - Data can be delivered by FTP or API

The product can be utilised by investors for active engagement as well as portfolio risk management. The controversies captured here also feed our ESG Assessments. To find out more, please contact Jordi Lesaffer (jordi.lesaffer@vigeo-eiris.com)

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V.E is a global leader in ESG assessments, data, research, benchmarks and analytics. Leveraging our extensive proprietary database, we equip market players with the ESG insight they need to manage risks and better understand and address their social and environmental impact. With a team of nearly 300 experts of 30 different nationalities, V.E is present in Paris, London, Brussels, Casablanca, Hong Kong, Milan, New York, Rabat and Santiago. Since 2019, V.E has been an Affiliate of Moody’s Corporation.

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