

SUSTAINABLE
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PROGRAMME



UNIVERSITY OF
OXFORD



Fossil fuel company Investor Relations (IR) departments and engagement on climate change

Briefing Paper
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About the Oxford Sustainable Finance Programme

The Oxford Sustainable Finance Programme at the University of Oxford Smith School of Enterprise and the Environment is a multidisciplinary research centre working to be the world's best place for research and teaching on sustainable finance and investment. The Programme was established in 2012 to understand the requirements, challenges, and opportunities associated with a reallocation of capital towards investments aligned with global environmental sustainability.

We research environment-related risk and opportunity across different sectors, geographies, and asset classes; how such factors are emerging and how they positively or negatively affect asset values; how such factors might be interrelated or correlated; their materiality (in terms of scale, impact, timing, and likelihood); who will be affected; and what affected groups can do to pre-emptively manage risk. We have conducted pioneering research on stranded assets and remain the only academic institution conducting work in a significant and coordinated way on the topic.

The production of high-quality research on the materiality of environment-related factors is a necessary, though insufficient, condition for these factors to be successfully integrated into decision-making. Consequently, we develop the data, analytics, frameworks, and models required to enable the integration of this information. We have particular expertise in asset-level data, spatial analysis, scenarios, and stress tests, and also focus on how information is presented and used.

We also research barriers to the adoption of practices related to sustainable finance and investment. This includes the role of policy, regulation, governance, incentives, behaviours, and norms in shaping investment decisions and capital allocation.

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Executive Summary

Investor Relations (IR) practitioners have three principal roles. Firstly, they serve a reporting function, and are responsible for reporting financial results to shareholders and the market. Secondly, they are responsible for hosting a number of key events for shareholders and stakeholders for both communication and marketing purposes. Finally, they also hold a strategic role—to varying degrees—in which they identify key emerging industry or market issues which may come to affect the company and/or its public reputation. Their role varies quite dramatically between companies, both in terms of their duties as well as their integration into the core functions of companies.

Many investors and civil society organisations want to compel companies, and particularly listed fossil fuel companies, to disclose information or take action on climate change. Both civil society and investors have tried to go directly to IR departments, often in a combative manner, to try to facilitate dialogue on such topics. This has been largely unsuccessful for three reasons. Firstly, because IR departments are very adept at deflecting criticism, and secondly, because IR workers themselves work under the specific mandate to prioritise requests from company shareholders. This means that civil society, which very seldom hold shares, are often ignored because of internal procedures that prioritise shareholders. Even in cases where civil society groups hold shares (or in the case of smaller investors), priority is given on the basis of the size of the shareholding. The third reason is that most IR departments have only been tasked with defending their company against criticism, rather than engaging in strategy. In other words, IR departments have for the most part been entirely reactive and defensive instead of proactive and strategic. Therefore, both civil society and smaller investors have been ‘boxed out’ by IR departments.

Investors and civil society should take a two-step approach to engagement. Firstly, they need to discern which companies’ IR teams are the most open to engagement, and secondly, they need a better understanding of the role of IR and the context of IR professionals in order to develop more nuanced and productive engagement strategies.

An arms race?

Civil society and investors have had only small successes in their engagement with fossil fuel companies on climate change. More sophisticated and multi-faceted strategies, including wide-scale partnering has begun, but could be expanded significantly.

However, as civil society and investors have been working together to create a climate-compatible future for today’s fossil fuel companies, some companies have been working hard on counter strategies. IR has become more responsive and more skilled at strategies that deflect attention away from climate change. Top management and IR teams have become more fluent in the language around climate change and this has also allowed them to become more nuanced in their communication.

The theories and practices adopted within IR departments and IR as profession are not static. They evolve over time, and seem to be evolving in response to greater NGO and investor engagement on climate change. IR departments are getting better at outmanoeuvring those seeking to force engagement and these changing strategies and tactics should be accounted for in the planning of future NGO and investor engagements.

Structural barriers in engaging IR teams on climate change

IR officers generally have a poor understanding of civil society and their role within the sector. Institutional norms within the IR industry present a number of structural barriers to engagement with listed fossil fuel companies on climate change.

Firstly, it needs to be said that IR officers, as is so common in other areas of industry, suffer from a ‘herd mentality’. We mean this not so much in a sense of group-think, but more to the effect that it is professionally difficult for them to break away from the mainstream conception of what IR’s role is within companies. Therefore, they feel it is personally risky to push an agenda such as climate change. The Investor Relations Society (IRS), a key industry body, is seen as the standard-bearer for maintaining and changing the professional norms within which IR operates, and could be a potential target for engagement to encourage greater accommodation of climate-related discussions and engagement with civil society within the industry.

Further, IR officers constantly feel under threat and view themselves as caught in the middle of a war on change. On the one hand, outside parties are constantly pressing for more action and disclosure on climate change issues. On the other hand, top management of fossil fuel companies tend to take a more conservative approach to any changes in favour of diversification or disclosure. There is often a wide gap between the climate change narrative communicated by the senior management of companies and the actual behaviour of businesses on the ground, which means IR officers are in a difficult position when communicating on such issues.

Demographics also appears to be a key determinant in the success of NGO and investor engagement with IR teams. Based on our interviews, the older and more experienced the head of IR is, the more cynical he or she tends to be about climate change issues. IR teams with a younger leader, or several younger members, including on closely related teams like sustainability, tend to be more receptive to climate change engagement.

Another aspect that civil society and investors need to be aware of is that IR officers are not just being approached by those who want more disclosure and action on climate change. IR teams are quite often exposed to a significant number of major shareholders who have the opposite view, and argue that major oil companies are not devoting enough resources to their traditional fossil fuel businesses. Cognisance of these differing viewpoints is important in building a relationship with the IR teams.

A strategy that civil society and investors say IR teams are using more regularly is deflection. This technique is used when investors and civil society ask difficult questions or press on certain divisive issues, including climate change. In this scenario, civil society and investors say IR teams routinely pass them over to dedicated sustainability teams. These teams specialise in communicating the company’s actions on climate change, but reportedly they often simply parrot the ‘corporate line’ to anyone who inquires. Many requests die at this stage as civil society and investors don’t know where else to push.

While we do not claim to have a comprehensive picture of all listed fossil fuel IR departments, some IR departments seem much more receptive to engagement than others. In particular, Total, Statoil, and BP all received positive comments from civil society and investors, saying that their IR and ESG (environmental, social and governance) teams had been open and helpful. Conversely, Royal Dutch Shell and ExxonMobil were reportedly very guarded, unresponsive, and were generally seen as trying to stymie the engagement process.

TCFD and opportunities for manipulation

The Task Force on Climate-related Financial Disclosures (TCFD) released their final recommendations in June 2017. The recommendations are primarily focused on generating forward-looking, scenario-based disclosures by preparers on climate-related risks.

The TCFD recommendations are, however, voluntary recommendations. This leaves a great deal of room to manoeuvre with the types of information that companies disclose. Many fossil fuel companies are likely to increase their amount of disclosure, but to do so in very self-serving and potentially manipulative ways, particularly in relation to scenarios. Companies could have a free hand in deciding which figures to publish, how they are calculated, and with little transparency regarding the assumptions they use. This could result in misleading figures which may only muddy the water further for investors.

The upstream energy industry suffers from a massive reporting gap already. There is a worrying disconnect between the importance of capex to the future performance of extractive companies, particularly international oil companies (IOCs), and ways that capex-related information is conveyed to investors via public disclosures and financial statements.

IOCs disclose data so broad and opaque that it is practically useless. For instance, many IOCs disclose their global or regional capex spending, but the information is so aggregated (e.g. 'EMEA capex spending'), that there is little useful information to be gleaned from a climate risk perspective (Rook & Caldecott 2015). One cannot see what specific projects the money was spent on, so it is almost impossible to judge environmental impacts or policy risk. In fact, the information given is so opaque, that it is not even possible to discern what the average capex spending is per project (Rook & Caldecott 2015).

It is not inconceivable that upstream fossil fuel companies could exploit the voluntary and non-universal nature of the TCFD recommendations to make an already poor reporting landscape even less transparent. The proposed use of climate-related scenarios in particular, create opportunities for disinformation and manipulation of disclosures that could confuse investors and other stakeholders.

The priority for investors and civil society

So how can investors and civil society combat this likely flood of disinformation? In our view, the best strategy will be to band together to require specific disclosures as well as the disclosure of assumptions for calculations, estimates, or projections. Where third-party frameworks or methodologies have been used when preparing disclosures, the type of framework or methodology used should also be disclosed.

Moreover, organisations developing frameworks or methodologies used by preparers should also disclose their assumptions. Where they fail to do so, investors and civil society should make clear that such frameworks or systems should not be used by preparers.

Together these principles would ensure that users of disclosure can compare like with like. This is fundamental to the guidelines being useful.

The principal near-term focus of engagement should therefore be on establishing these principles for the disclosure of assumptions. It is likely that only a united and assertive voice from investors will be sufficient to get companies to disclose transparent and comparable information.

In addition to engaging with companies themselves, we also believe investors and civil society should focus their efforts on working directly with IR professionals by pursuing collaboration with the major industry groups for the profession: the Investor Relations Society in the UK and the National Investor Relations Society (NIRI) in the US. By seeking out more and better training opportunities, investors and civil society can help deliver on short- and long-term goals for a change in thinking and approach both from IR professionals and the companies they represent now and in the future.

Furthermore, investors and civil society need to be prepared to engage directly with ever more climate-savvy management and board members. As highlighted by Exxon's move in December 2017, many firms are giving shareholders direct access to board members (*Financial Times*, 2017). While this may present an opportunity for engagement, especially at the outset, we believe such access will sharpen the manipulative powers of board members and perhaps harden their stance to climate discussions. Accordingly, unity and pressure are the key tactics investors and civil society must adopt to enact change.

Introduction

This Briefing Paper reviews the roles and behaviours of Investor Relations (IR) functions in listed fossil fuel companies, particularly those listed in London. It is based on an ongoing study that seeks to illuminate the poorly understood role of IR teams in the context of climate change engagement. The project has been conceived as a way to help improve efforts to engage with listed fossil fuel companies on climate change, particularly by civil society and investor coalitions. These engagement efforts have increased significantly over recent years.

The paper provides an overview of IR, gives insight into IR professionals themselves, and sets out how civil society and investors can develop strategies that could lead to more productive engagement with fossil fuel companies through their IR departments.

IR is currently poorly covered in academic and industry literatures, and given that IR is a potentially important link in the engagement chain, research into this area has never been more needed. IR teams have well-established links to senior management and are a key gatekeeper, meaning they may prove an enabler or barrier to effective engagement on climate change with company management.

This study is primarily interview-based and has comprised semi-structured interviews with IR officers, civil society professionals, and institutional investors. The project began with a roundtable in mid-June 2017 which was attended by a number of investors and civil society representatives. The research team has since held interviews to test the hypotheses of the project. The findings outlined here are based on the evidence we have so far collected from our interview process with industry insiders between June and November 2017.

It should be emphasised that the authors are not making the case that the best way to change upstream fossil fuel companies is via their IR departments. Rather, given that civil society and investors concerned with climate change are in the midst of ramping up engagement with fossil fuel companies, we feel it is important to set out how IR works and what the opportunities might be for more effective engagement with them.

What are IR departments and how do they work?

IR is the communication of information and insight between a company and the investment community (IRS, 2017). Generally speaking, IR practitioners have three principal roles. Firstly, they serve a reporting function, and are responsible for reporting financial results to shareholders and the market. Secondly, they are responsible for hosting a number of key events for shareholders and stakeholders for both communication and marketing purposes. Finally, they also hold a strategic role—to varying degrees—in which they identify key emerging industry or market issues which may come to affect the company and/or its public reputation.

Their role varies quite dramatically between companies, both in terms of their duties as well as their integration into the core functions of companies. We shall cover this variation in duties later in this briefing.

In general, there are four different engagement points between investors and IR teams. These include:

- *Quarterly announcements* – these have a sell-side¹ focus. They are organised by IR teams and have high-level management on the call.
- *Set piece roadshows* –with high-level management usually in attendance, but often led by the corporate broker² community. IR teams attend and prepare the packs/materials, set the agenda and prioritise which individual investors the management should meet. These are often sector-driven (e.g. oil and gas, telecoms, or consumer goods) roadshows, so content on ESG will vary.
- *Management meetings with investors* – tend to occur with the largest investors, and can be one-on-one or a group of individual investors in attendance.
- *Ad hoc queries* – IR teams can field these, or can pass them on to the relevant teams within the company. This is key for equity research analysts, who will have regular calls and updates from IR contacts regarding the stocks they are involved in.

IR's organisational position within companies varies considerably, but they are usually a department under the remit of the Chief Financial Officer (CFO). The degree to which they are integrated into the core functions of companies differs widely, with some IR departments intimately connected into operational aspects (e.g. project financing, technical aspects of exploration and production³ etc) and others functionally 'siloes' off from the rest of the business. IR officers spend the majority of their time focusing on quarterly results reporting and key communication events with shareholders, equity research analysts, and asset managers. Generally, their explicit focus is on serving shareholders and answering requests from that group; those who do not hold shares, or without a direct influence on shares generally, receive little attention.

¹ Sell-side refers to the part of the financial industry that is involved in the creation, promotion and sale of stocks, bonds, foreign exchange and other financial instruments. (Investopedia.com, 2017)

² Corporate brokers advise companies on fund raising (e.g. new issues of shares), are knowledgeable about the share and other financial markets. They try to generate interest among investors for the company's securities. They also buy and sell companies' shares. (London Stock Exchange, lse.co.uk, 2017)

³ Synonymous with 'upstream', exploration and production (commonly referred to as E&P) is a specific sector within the oil and gas industry focused on finding, augmenting, producing and marketing different types of oil and gas. (Investopedia.com, 2017)

Is IR significant for changing fossil fuel company behaviour on climate change?

IR departments often mediate the dialogue between companies, investors and other external stakeholders, including civil society. Yet civil society in particular, and many investors, have a poor understanding of investor relations and how IR departments operate. Many participants in this research questioned IR departments' capacity to influence real change within a fossil fuel company, with others querying whether it was worth exploring this actor group at all in relation to climate-related engagement. Given their gate-keeper role and a widespread lack of understanding about their role, we believe that this is an important opportunity to help clarify the interests, incentives and impact of IR departments. There are a number of particularities about the IR function we seek to clarify here which speak to the significance of IR departments in sparking change.

Many civil society organisations and investors want to compel companies to disclose information or take action on specific topics. In order to accomplish this, both have gone directly to IR departments, often in a combative manner, to try to facilitate action and dialogue. This has been largely unsuccessful for three reasons. Firstly, because IR departments are very adept at deflecting criticism, and secondly, because IR workers themselves work under the specific mandate to prioritise requests from company shareholders. This means that civil society, which very seldom holds shares, are often ignored because of internal procedures that prioritise shareholders. Even in cases where civil society does hold shares (or in the case of smaller investors), priority is often based on the size of the shareholding. The third reason is that most IR departments have been tasked with defending their company against criticism, rather than engaging with opportunities for strategic moves to propel it forward. In other words, IR departments for the most part are reactive and defensive instead of proactive and strategic. Therefore, both civil society and smaller investors are often 'boxed out' by IR departments. Many participants in our research commented that they had given up on IR engagement, believing that it was unlikely to spark further behaviour change, and tended to speak either directly to corporate management if they had access, or to the corporate sustainability team.

The method of engagement adopted by investors and civil society, where they do engage, has developed in such a way that it can create conflicts of interest for IR teams, particularly those without a strategic mandate. Engagement efforts therefore often fail to efficiently utilise the structure of companies and the mandate of different internal teams to their advantage. Accordingly, many attempts to change company behaviours have failed to gain a foothold at a suitable corporate level, losing momentum quickly as they encounter institutionalised barriers within corporate structures, with efforts often failing to erode undesirable practices and processes. This suggests that the significance of IR teams in effecting corporate change will largely depend on their internal mandates, rather than the degree of engagement. To some degree, then, this is not entirely the fault of IR departments or even of companies, and we will now outline some opportunities to reframe and reconsider engagement with IR departments to pursue future opportunities for impactful engagement.

The subdivisions of IR must be further differentiated to better speak to the significance of IR departments in affecting behaviour on climate change. Companies often have separate teams for equity-related IR and debt-related IR, and while neither side generally receives high marks from investors or civil society, the debt side of IR tends to be more friendly to climate-oriented discussion and therefore more likely to be aligned with creating behaviour change. With the long-term nature of fossil fuel project financing and the even longer-term maturities of many bonds, there is little of the short-termism that complicates equity IR. Investors tend to be more engaged and have fewer conflicts of interest on the fixed income side than on equity. In equities, there are often dichotomous short- and long-term goals. For example, investors asking a company to raise dividends may work against long-term term goals, complicating requests. Other investors might ridicule investment in renewables or other climate-friendly activity, putting equity IR teams in a difficult position of balancing conflicting investor interests and demands. However, on the debt side, asking a company how it plans to deal with issues on a 30-year project financing horizon is perfectly aligned with both fiduciary and climate interests, so there are potentially fewer roadblocks to dialogue.

Consequently, we suggest that investors and civil society take a two-step approach to increase the efficiency and impact of engagement efforts. Firstly, they need to discern which companies' IR teams are the most open to engagement, and secondly, they need a better understanding of the role of IR and the context of IR professionals in order to develop more nuanced and productive engagement strategies.

To illustrate the point of how different types of engagement may be more or less successful, here is an example from an NGO that has been seeking to engage with fossil fuel companies for over half a decade. In the beginning years of their work their main strategy was to try to get press attention that scolded fossil fuel companies for not doing more; in their words, a 'name and shame' strategy. The more stories that were written, the more successful they considered themselves as they believed the publicity would force the companies in question to change.

However, that simply did not occur. By chance, this NGO linked up with a medium-to-large investor who held shares in a major fossil fuel company. The NGO utilised the investor's position to secure discussions and meetings with the IR team in question, and then in turn helped the investor to ask intelligent and more nuanced questions. The success of this engagement – which has evolved over more than two years into a relationship that consists of more than six meetings a year and has led to tangible change in company behaviour (e.g. information-sharing and 'open ears' to suggestions) – made the NGO completely reconsider its strategy.

This NGO-investor partnership model has been leveraged by a handful of others as well. It has been successful in sparking change in fossil fuel company behaviours so far for three primary reasons. Firstly, by operating within the mandate of IR teams to prioritise requests from company shareholders, it utilises the size and scale of the investor to compel discussions. Secondly, it allows investors access to the extensive knowledge base that civil society possesses on climate change topics. Thirdly, because investors 'speak the language', they can digest and reframe civil society's questions and concerns in a fashion that promotes a more positive response from IR officers.

Civil society can make use of investor-IR meetings in numerous other ways as well. One of the critical aspects is learning about company information that has not been publicly disclosed. This intelligence gathering purpose covers a range of possible topics, but an example might be a forthcoming report that a fossil fuel company is putting out on a given topic, allowing an NGO or investor coalition to plan their response in advance. Importantly, this knowledge-sharing practice can become a dialogue, with civil society able to win favour with IR professionals by also acting as an information source. By directing the company to other pertinent reports or materials or fielding general inquiries that speak to the expertise and skills of the NGO, they can make themselves relevant and helpful. This can be positive for relationship- and dialogue-building, but could also allow the civil society groups to influence the corporate report directly, potentially influencing perceptions of the topic within the company and the wider fossil fuel and investment industries.

This section has outlined ways in which engagement with IR departments can, but does not necessarily, have a significant impact on changing corporate behaviours relating to climate change. However, this should come with a disclaimer: we recognise that IR departments are not the only target for engagement, and might actually not be the right one, particularly for those civil society groups who are not shareholders (or working in partnership with investors). Direct engagement with company management, for example, might be more significant in catalysing change. Rather, we highlight that the significance of IR departments in changing corporate behaviours will vary from company to company, based on the type of organisation that is engaging with and through the IR department. This briefing paper does recognise that they are a vital part of the communication chain within fossil fuel companies, so should be better understood by those interested in these themes, and do have the potential to have an impact on corporate behaviours.

How is IR practised and how is it responding to climate change?

The theories and practices that IR departments (and IR as a broader profession) adopt are not static. They evolve over time as economic landscapes, markets and industry norms change, and they seem to be evolving in response to greater NGO and investor engagement on climate change. IR departments are getting better at out-maneuvring those seeking to force engagement and these changing strategies and tactics should be accounted for in NGO and investor engagements that are being planned.

Over the last three years there has been a significant increase in the responsiveness and sophistication of fossil fuel company management on climate change issues. In particular, corporate management has become more attuned to the overall importance of the topic both in the public eye, but perhaps more crucially, among institutional investors. IR departments are being increasingly deployed to pay special attention to investor and NGO sentiment in this area. Yet this has also meant that the capacity of both management and IR departments to deflect and hinder engagement has grown considerably. It appears that there is a strategic arms race developing over climate change disclosure, but there are ways that civil society and investors can tactically engage to produce positive outcomes. We will thus outline the role of IR and provide insight into the professionals who practise it, as well covering how civil society and investors can best work with them to facilitate engagement.

Investor relations within fossil fuel companies is practised in much the way that it is in other sectors, except that IR professionals tend to have a sharper focus on environmental issues, the 'E' in ESG, than in other industries, and especially in the last three to four years. One of the key operational differences between companies is where ESG issues are officially handled. Almost all companies now have designated ESG officers, but depending on the company they either sit in a stand-alone ESG division, or they are integrated into the IR team, with the ESG officer reporting to the head of investor relations, who in turn reports to the CFO.

In the latter arrangement, ESG tends to play a very strategic role in IR operations, as it serves as both an outward-facing and inward-facing gatekeeper. It is outward-facing in the sense that it serves as a filtering channel for key industry information on ESG, but it is also inward-facing as it remains a vital communication mechanism between IR and the company as whole. This is because its broad remit to understand company operations ties it into the whole of the business rather than investor relations alone, which has a narrower, outward-looking focus. ESG can therefore be a two-way channel where information can flow from the outside world into the company and from the company outward. Different companies have particular arrangements, with Shell and Statoil seen as particularly progressive on environmental issues and ESG integration, while Exxon-Mobil is seen as a laggard by climate professionals. Generally speaking, when ESG is formally integrated into IR, environmental issues seem to be taken more seriously by the company. By this we mean that IR teams are less dismissive of climate change issues and are more open to dialogue, as opposed to when ESG is not integrated, in which case IR becomes a brick wall that attempts to block engagement.

Building on the connection between ESG and IR, investor relations can be a key conduit for reaching and influencing senior management of companies. IR officers routinely hold meetings with the CEO and CFO and are seen internally as holding an important strategic role, so the escalation of environmental issues through the ESG→IR→CFO channel can be important, although this is shown through our interviews to be company specific.

In terms of engagement, IR officers generally have a limited understanding of civil society and its role within the sector. The few that do understand civil society generally hold a poor opinion of them as they are usually approached in a combative manner. IR officers are usually held to a strict corporate policy of responding quickly to requests from shareholders, so when civil society do get in contact, they are usually very low on the priority list. For investors, the situation is different, as depending on their size and the volume of shares they hold, they are given varying amounts of attention, and in some cases, in-person meetings and phone calls. For both civil society and investors, understanding the mind-set of IR officers may greatly enhance the success of their

engagement strategies. We now outline a number of insights garnered from our interviews that could aid engagers better understand the IR professionals they encounter.

Firstly, it needs to be said that IR officers, as is so common in other areas of industry, suffer from a ‘herd mentality’. We mean this not so much in a sense of group-think, but more to the effect that it is professionally difficult for them to break away from the mainstream conception of what IR’s role is within companies. Therefore, they feel it is personally risky to push the envelope on the climate front. The Investor Relations Society, a key industry body, is seen as the standard-bearer for maintaining and changing the professional norms within which IR operates, which means they could themselves be a target for engagement by civil society to try to shift industry-wide norms and levels of education on climate topics.

Further, IR officers constantly feel under threat from investors and other groups as they view themselves as caught in the middle of a war on change. On the one hand, outside parties are constantly pressing for more action and disclosure on climate change issues. On the other hand, top management of fossil fuel companies tend to take a more conservative approach to any changes in favour of renewable energy or disclosure. This dichotomy between the demands of external shareholders and stakeholders and that of internal management, who are the managers of IR professionals themselves, puts IR officers in a very difficult position. While their job is to communicate with shareholders and the public, they have little personal incentive to offer much help to those seeking positive action on disclosure or climate change generally. Their position is also made more difficult by the complex reality of the companies they represent. There is often a wide gap between the climate change narrative communicated by the senior management of companies and the actual behaviour of businesses on the ground, which means IR officers can be in an awkward position when communicating on such issues.

Age is also a key determinant in the success of NGO and investor engagement with IR teams. Based on our interviews, the older and more experienced the head of IR is, the more cynical he or she tends to be about climate change issues. IR teams with a younger leader, or several younger members, including on closely related teams like sustainability, tend to be more receptive to climate change engagement.

Civil society and investors should also be aware that IR officers are not just being approached by those who want more disclosure and more investment in renewables. There are a significant number of major shareholders who have the opposite view, and argue that major oil companies are not devoting enough resources to their traditional fossil fuel businesses and/or the provision of short-term returns and dividends. This means the IR officer is once again stuck in the middle, trying to cater to both parties, but ultimately failing to satisfy either.

The lack of receptiveness around climate is therefore a result of both internal mandates and incentive structures, as well as mixed messaging from investors. While investors understandably have different requests of companies, there is currently little organisation among investors who do share similar views, making it time-consuming and difficult for companies, and specifically IR professionals, to respond in a coordinated way. Add to the mix the reality that investors are simultaneously often making contradictory demands – like ‘increase the dividend’ or ‘generate more free cash flow’ at the same time as ‘commit more R&D money to renewables’ – and it becomes apparent that the difficult position of IR professionals is clearly partly of investors’ and civil society’s making. Ideally, to overcome this issue, an NGO could partner with a number of investors to design common questions/requests that they would like to communicate to companies, as has become common at larger organisations in recent years, particularly through the efforts of the Aiming for ‘A’ Investor Coalition. This type of partnered engagement can often promote a quicker and more comprehensive response from fossil fuel companies. This engagement strategy has had some success, but one of its significant deficiencies is that because climate change goals are so heterogeneous between different civil society groups and investors, consortium-based requests usually suffer from a ‘lowest common denominator’ problem. This problem stems from the fact that consortiums can only lead with points that all parties agree on, which usually considerably limits the scope of such demands.

So far such strategies have had limited success as they have been parried by a number of counter strategies. Our interviews from the NGO and investor side reported that these strategies include hollow rhetoric, deflection, and

‘cherry-picking’ by companies and their IR teams. Hollow rhetoric refers to the increasing tendency of top management and IR teams to focus on broad discussions of climate-friendly outlooks and initiatives, which are supported by very little or no action. This strategy creates positive press coverage for companies but in reality involves little change. Civil society and investors said the tactic was clever because it was hard to fully ascertain whether their efforts were indeed ‘green-washing’ or not until they had spent considerable time communicating with a company. However, through the engagement process, civil society and investor said they intermittently came into contact with teams in areas such as exploration and production (E&P), and in those dialogues, it quickly became apparent to them that the operational architecture of the oil business had not changed despite years of rhetoric about renewable energy goals. That said, some companies, like Total, were reported to have been much more proactive, while others, like ExxonMobil, have been laggards.

Another IR strategy civil society and investors say IR teams are using is deflection. This technique was used when investors and civil society asked difficult questions or pressed on certain climate issues. In this scenario, civil society and investors say IR teams routinely passed them over to dedicated sustainability teams. These teams specialise in communicating the company’s actions on climate change and renewables, but they reportedly often simply parrot the ‘corporate line’ to anyone who inquires. Many requests die at this stage as civil society and investors don’t know where else to push.

While we do not have a comprehensive picture, some IR departments seem much more receptive to engagement than others. In particular, Total, Statoil, and BP all received high marks from civil society and investors, saying that their IR and ESG teams there had been open and helpful. Conversely, Royal Dutch Shell and ExxonMobil were reportedly very guarded, unresponsive, and were generally seen as trying to stymie the engagement process.

The future of IR

As has become apparent in this report, both civil society and investors have had only small successes in their engagement with fossil fuel companies. More sophisticated and multi-faceted strategies, including wide-scale partnering has begun, but could be expanded significantly. However, just as civil society and investors have been working together to create a more climate-friendly future for the fossil fuel industry, companies themselves have been working hard on counter strategies. As much as management and IR has become more responsive, they have also become more skilled at strategies which deflect attention away from climate change. Top management and IR teams have become more fluent in the language around climate change, but this has also allowed them to become more nuanced in their communication.

Though the recommendations of the Task Force on Climate-related Financial Disclosures (TCFD) were only released in June 2017, the TCFD has been shaping actions on both sides of the disclosure fence for at least two years (TCFD 2017). The final recommendations demand a robust package of disclosures that are primarily based on scenario analysis by issuing companies on how climate risks will affect their businesses. They are, however, currently only voluntary recommendations. This leaves companies a great deal of room to manoeuvre over the types of information that they can disclose. Our research indicates that many companies are likely to increase their amount of disclosure, but do so in very self-serving and potentially manipulative way, particularly in relation to scenarios. Companies and IR teams could have a free hand in deciding which figures to publish, together with how they are calculated, and there could be little transparency in relation to the assumptions they use. This will be likely to result in misleading figures which may only muddy the water further for investors, but provide greater freedom for IR teams to evolve their climate communication.

The analogue for this type of free-wheeling disclosure can be seen in publicly-traded technology stocks and the stock market as a whole. Many major tech businesses release two forms of earnings. The first set are the so-called GAAP (Generally Accepted Accounting Principles) figures, which disclose their financial results in line with the standard method mandated by the US Internal Revenue Service and Securities and Exchange Commission (SEC 2016). However, the IR teams at these companies seek to create market hype by turning the focus to a very different set of earnings—non-GAAP earnings. Technology companies have thus developed their own methods and metrics to present financial results. Some of these have been even be standardised across the sector, but many are done on a company-specific basis. These non-GAAP earnings present information in often quite misleading ways, and fossil fuel companies seeking to ‘disclose’ more on climate change and broader ESG issues could replicate these tactics.

Using non-GAAP earnings is prevalent in the technology sector, including 80% of technology companies in the S&P 500 (Bloomberg 2016). For instance, many tech companies disclose profit figures that do not fully account for various costs that are integral to their operations. Shake Shack, for example, publishes its profit figures without including its new store opening costs (Bloomberg 2017), an action even the company’s CFO has admitted may limit the usefulness of this metric. Facebook releases ‘pro forma’ earnings (another term for non-GAAP earnings) that significantly distort performance metrics, for example by removing the payroll taxes it pays on employee stock options. In 2015, this action made their non-GAAP earnings \$6.5bn or 78% higher than their GAAP earnings (Bloomberg 2016). Salesforce strips out equity compensation for employees, the costs for buying new assets, and provides a reworked version of taxes it paid. In 2015, this turned a \$47m annual loss into a \$507m profit (Bloomberg 2016). In aggregate, this practice has a very distorting effect on tech valuations, with the discrepancy between GAAP earnings and preferred non-GAAP earnings amounting to \$45bn a year, or a 23% margin (Bloomberg 2016).

Making the situation worse, the equity research industry has often bought into these nuanced methodologies and many analysts and investors make investment decisions based on the non-GAAP figures being broadcast by the IR departments of technology companies (Bloomberg 2016). Worse yet, non-GAAP earnings have started to seep into many important financial databases used by investors, such as FactSet, which now includes non-GAAP earnings in its data (Bloomberg 2016). On the whole, the use of non-GAAP earnings is still proliferating, and can

be argued to be distorting the valuation of the entire market. This demonstrates the power of IR and corporate reporting strategies, and the importance of corporate engagement to gain a clearer understanding of corporate strategy and performance through open dialogue and the opportunity to question reporting data.

Arguably the upstream energy industry suffers from a massive reporting gap already. There is a worrying disconnect between the importance of capex to the future performance of extractive companies, particularly international oil companies (IOCs), and ways that capex-related information is conveyed to investors via public disclosures and financial statements. The current practice is to report capex only in an aggregated way, making it impossible to determine how capex is distributed across projects. This leaves investors in the dark about how risky investments in extractive companies are. In this way, the behaviour of oil companies is similar to technology companies (i.e. the use of misleading information), but the strategy they use is different and more opaque.

For example, while technology companies' figures are significantly re-engineered to create a positive picture, the companies at least disclose all the assumptions and the methodologies they used to create those figures. So, while the data may not be standardised, investors can at least know what sort of data they are dealing with. This is different to IOCs, which give data so broad and opaque that it is practically useless. For instance, many IOCs disclose their global or regional capex spending, but the information is so aggregated (e.g. 'EMEA capex spending'), that there is little useful information to be gleaned from a climate perspective (Rook & Caldecott 2015). One cannot see what specific projects the money was spent on, so it is near impossible to judge environmental impacts. In fact, the information given is so opaque, that it is not even possible to discern what the average capex spending is per project (Rook & Caldecott 2015).

Using this habitual opacity as a base, it is not inconceivable that upstream fossil fuel companies could exploit the voluntary and non-universal nature of the TCFD recommendations to make an already poor reporting landscape even less transparent. The proposed use of climate-related scenarios in particular, creates opportunities for disinformation and manipulation of disclosures that could confuse investors and other stakeholders.

Scenario analysis as a technique is well used in the corporate world, and has been for several decades (TCFD 2017). However, even without the intent to manipulate, the technique has been shown to have serious issues (McKinsey 2017). For instance, corporate managers consistently underestimate the potential impact of future events on costs or market prices, or over-discount the likelihood of events occurring in the first place (McKinsey 2017). Extreme scenarios are often excluded from analysis because 'they won't happen', and even if they do, 'all bets are off', according to McKinsey (2017). This discounting of both the likelihood and severity of events occurs despite numerous real-world examples occurring frequently (e.g. the 2010 Deepwater Horizon explosion, 2011 Fukushima disaster, or geopolitical issues like Germany's *Energiewende*). When you add the intent to mislead into the mix, then scenario analysis looks like a particularly ripe area for misinformation.

The TCFD mandates that the scenarios companies analyse should be 'plausible, distinctive, consistent, relevant, and challenging' (TCFD 2017). However, these are significantly open to interpretation—deciding what is 'plausible' or 'reasonable', for instance—which leaves room for manipulation. For example, a company could use a climate-change projection scenario to demonstrate the robustness of its current reserves, but not disclose any assumptions, making comparison with its peers impossible. It may project a 3°C future temperature, for instance, but hide within that projection that they have not assumed any change in future energy prices despite the high likelihood of more regulation and government support of renewables in such a scenario. In this way, they could make their business appear more defensible and sustainable than is reasonable.

The TCFD says that the real value of scenario analysis is in looking at the ways that various factors interact with one another. However, that can make the whole exercise very vulnerable, as if one underestimates a single factor, it can significantly change the whole set of analysis. For example, in projecting a high temperature change scenario, if one does not assume any future changes in regulation, which seem a certainty given the likely high degree of public reaction in such a situation, then that can affect a whole host of other factors, such as supply and demand for fossil fuels, emissions pricing, or tax-related incentives/penalties related to electric or fossil fuel cars and machines. In this way, we believe that the TCFD's scenario analysis may simply open the door to more

disinformation from IOCs and opportunities for IR departments to create positive news and disclosures while underplaying the systemic risks in their firm.

Recommendations

So how can investors and civil society combat this likely flood of disinformation? In our view, the best strategy will be to band together to require specific disclosures as well as the disclosure of assumptions for calculations, estimates, or projections. Where third-party frameworks or methodologies have been used when preparing disclosures, the type of framework or methodology used should also be disclosed.

Moreover, organisations developing frameworks or methodologies used by preparers should also disclose their assumptions. Where they fail to do so, investors and civil society should make clear that such frameworks or systems should not be used by preparers.

Together these principles would ensure that users of disclosure can compare like with like. This is fundamental to the guidelines being useful.

The principal near-term focus of engagement should therefore be on establishing these principles for the disclosure of assumptions. It is likely that only a united and assertive voice from investors will be sufficient to get companies to disclose transparent and comparable information.

In addition to engaging with companies themselves, we also believe investors and civil society should focus effort on working directly with IR professionals by pursuing collaboration with the major industry groups for the profession: the Investor Relations Society in the UK and the National Investor Relations Society (NIRI) in the US. By seeking out more and better training opportunities, investors and civil society can help deliver on short- and long-term goals for a change in thinking and approach both from IR professionals and the companies they represent now and in the future.

Furthermore, investors and civil society need to be prepared to engage directly with ever more climate-savvy management and board members. As highlighted by Exxon's move in December 2017, many firms are giving shareholders direct access to board members (*Financial Times*, 2017). While this may present an opportunity for engagement, especially at the outset, we believe such access will sharpen the manipulative powers of board members and perhaps harden their stance on climate discussions. Accordingly, unity and pressure are the key tactics investors and civil society must adopt to enact change.

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