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CCUA
Canadian Credit Union Association

REPORT

# Risk Management's New Tool: Corporate Social Responsibility

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## Acknowledgments

Filene thanks our generous supporters for making this important research possible.

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# Executive Summary

### Overview

Corporate social responsibility can help credit unions proactively manage systemic risk. In this way, credit unions will achieve greater impact within their communities.

MEET THE AUTHOR

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Cooperative governance. Member-centric decisions. Strong and authentic ties to their communities. All credit unions exhibit these and other facets of corporate social responsibility (CSR)—it is core to their DNA and their reason for being. Many credit unions now also proactively manage the CSR aspect of their business, in order to achieve greater impact, attract members and employees, reduce costs, grow revenues, and build their brand and competitive differentiation. But while CSR is laudable and worth pursuing for its own sake, we seek to understand other ways it can contribute to the success of credit unions and their members.

### What Is the Research About?

Seven credit unions with strong CSR practices—three from the United States and four from Canada—were interviewed in this study for their views, practices, and results in harnessing CSR as a risk mitigation tool. We also explored public reports to see how large banks are using CSR to address risk.

Because credit unions already have well-understood risk areas, we open up each of the following in search of CSR connections: credit risk, liquidity risk, operational risk, reputation risk, strategic risk, regulatory risk, systemic risk, and market risk. For each of these risks, participating credit unions were asked whether and how CSR could improve their risk profile. In cases like reputation, regulatory, and operational risk, CSR holds clear present value. In others, like credit and market risk, interviewees agree about the potential, though the connections are less obvious. Possibly, CSR can help improve systemic risk, but only through sustained collective efforts.

A list of credit union CSR best practices rounds out the recommendation section.

### What Are the Credit Union Implications?

We identify four stakeholder groups that should take note of this report's findings:

- **Credit union boards.** Hold a governance-level discussion about how CSR should be integrated into your business strategy. Make sure your CSR objectives and the supporting metrics are clear, well understood, and embedded throughout the organization.

- **Risk and credit officers.** Invite those responsible for CSR into risk management conversations. Pay attention to emerging CSR practices at larger institutions and among peers. Develop and test theories relating CSR to your risk profile.
- **CSR managers.** Learn the language of risk management, including categories, tolerances, and outcomes. Quantify your activities so they can more easily be used in risk models. Understand how social and environmental trends can become risks and opportunities for your credit union.
- **Credit union system leaders.** Aggregate data on the CSR activities of credit unions in your jurisdiction. Start with one or two metrics to allow for broader reporting for public and regulatory consideration. Articulate how collaborative CSR among credit unions can ameliorate systemic risk.

Whether you are teaching financial capability courses, lending to renewable energy companies, updating your environmental impact policies, or making your credit union a more inclusive employer, CSR can help mitigate your risks.

FIGURE 1

### RISK CATEGORIES USED IN THE STUDY

| |
|---|
| Credit risk: The risk of loss arising from the inability or failure of a borrower or counterparty to meet its obligations. |
| Liquidity risk: The potential inability of the credit union to meet contractual or contingent financial obligations, either on or off the balance sheet, as they come due. |
| Operational risk: The risk of loss or harm resulting from inadequate or failed internal processes or systems, or from people or external events. |
| Reputation risk: The risk that an action, transaction, investment, or event will reduce the trust that members, employees, or the broader public has in the credit union's integrity or competence. |
| Strategic risk: The risk that the enterprise or particular business areas will make inappropriate strategic choices, or will be unable to successfully implement selected strategies or related plans and decisions. Business strategies include merger and acquisition activities. The risk of a loss that results in a decline in a credit union's competitive edge. |
| Regulatory risk: The risk that the credit union will violate a regulation or that a change in laws and regulations will materially impact the credit union. |
| Systemic risk: The risk that the financial system will be put in real and immediate danger of collapse or serious damage with the likelihood of material damage to the real economy, and that this will result in financial, reputation, or other risks. |
| Market risk: The impact of market prices on the financial condition of the credit union. |

# Risk Management's New Tool: Corporate Social Responsibility

CHAPTER 1

## Introduction

Credit unions may have a silent weapon in their risk management arsenal: corporate social responsibility (CSR).

As credit unions build their risk management and CSR management capabilities, they are well positioned to tap into higher levels of social impact and financial success. However, the correlation between these two strategies—CSR and risk management—is not well known or understood. To determine if this win–win is achievable, credit union boards, managers, and risk and CSR professionals need to become familiar with this potentially symbiotic relationship. The aim of this report is to unpack these connections and to further define the ways in which CSR is or can be a risk mitigation strategy for credit unions.

*This report explores the question: Can credit union social responsibility be leveraged as a risk mitigation strategy?*

CHAPTER 2

# Methodology

Seven credit unions—three from the United States (one a segment-based credit union) and four from Canada—were interviewed in this study for their views, practices, and results in harnessing CSR as a risk mitigation tool. These credit unions were selected because of their strong CSR practices. They include:

- Assiniboine Credit Union (Canada)
- Affinity Credit Union (Canada)
- Servus Credit Union (Canada)
- Vancity Credit Union (Canada)
- Affinity Plus Federal Credit Union (United States)
- First Tech Federal Credit Union (United States)
- Redwood Credit Union (United States)

Interviews were conducted in the fall of 2015 with two or more credit union leaders at each organization, with diverse roles, including CEOs and VPs or managers of finance, treasury, credit, wealth management, business banking, risk, marketing and communications, operations, human resources, community investment, and CSR.

A scan was also conducted of the 2014 CSR reports of four large Canadian and American banks (RBC, TD, Bank of America, and JPMorgan Chase) to assess the degree to which banking competitors consider CSR as a risk tool.

## Definitions

In order to consider the connections between CSR and risk, it is important to first define these two terms. The interviewees agreed on the following definitions for the purpose of the research.

## Corporate Social Responsibility

Credit unions adopt different terminology for their CSR approach, including *values-based banking*, *doing the right thing*, *social purpose*, *impact*, *community*, *CSR*, and *sustainability*. Regardless of the terminology, the interviewed credit unions have fairly consistent definitions of CSR.

CSR is the creation of positive economic, social, and environmental impact through business. It covers governance, products and services, community and employee well-being, and environmental impacts. It is a process of integrating the organization's social purpose and, in particular, its concerns about healthy members, employees, communities, and the environment into the institution's decision-making process. Many credit unions use CSR as a business strategy and include CSR goals in their business plans.

This definition of CSR is used throughout the report. See the appendix for a list of credit-union-specific CSR practices.

## *How Banks Define CSR*

### RBC

"At RBC, we think of corporate responsibility, or citizenship, as an approach to business in which we work to make a positive impact on society, the environment and the economy."[1]

### Bank of America

"Corporate Social Responsibility permeates every part of our company, including business policies and practices, services and products, and employee benefits, in addition to public policy, philanthropy, volunteerism and community outreach. CSR is embedded in our governance, is one of the key ways we identify risks and opportunities, and plays a critical role in our business strategy of responsible growth."[2]

### JPMorgan Chase

"We strongly believe in being a good corporate citizen. We are one of the most philanthropic companies in the world (we give away more than $200 million a year), but we are able to do much more than provide money. We bring the skills, resources and global knowledge of our entire firm to support the economic growth and progress of communities across the globe."[3]

### TD

"TD's approach to Corporate Responsibility focuses on four key themes: responsible banking, building an extraordinary workplace, be an environmental leader, strengthen our communities."[4]

## Enterprise Risk Management

While there are some slight differences in how the sample credit unions organize and prioritize their enterprise risks, the common risk categories used in this study are:

- **Credit risk.** The risk of loss arising from the inability or failure of a borrower or counterparty to meet its obligations.
- **Liquidity risk.** The potential inability of the credit union to meet contractual or contingent financial obligations, either on or off the balance sheet, as they come due.
- **Operational risk.** The risk of loss or harm resulting from inadequate or failed internal processes or systems, or from people or external events.
- **Reputation risk.** The risk that an action, transaction, investment, or event will reduce the trust that members, employees, or the broader public has in the credit union's integrity or competence.
- **Strategic risk.** The risk that the enterprise or particular business areas will make inappropriate strategic choices, or will be unable to successfully implement selected strategies or related plans and decisions. Business strategies include merger and acquisition activities. The risk of a loss that results in a decline in a credit union's competitive edge.
- **Regulatory risk.** The risk that the credit union will violate a regulation or that a change in laws and regulations will materially impact the credit union.
- **Systemic risk.** The risk that the financial system will be put in real and immediate danger of collapse or serious damage with the likelihood of material damage to the real economy, and that this will result in financial, reputation, or other risks.
- **Market risk.** The impact of market prices on the financial condition of the credit union.

For each of these risks, participating credit unions were asked whether or not CSR (using the general definition given above) can be a useful mitigation tool. They were also asked for success stories and metrics that illustrate the risk benefits of CSR. These interviews form the basis of this report, supplemented by the author's experience and approaches banks are taking on this topic, as disclosed in their CSR reports.

A summary of the results from this ground-breaking research begins in Chapter 3, which nests the study findings in a global analysis of the business and banking benefits of CSR. Chapter 4 provides a detailed look at whether and how CSR can mitigate each of the eight risks. The report concludes with recommendations to credit union boards and managers and the overall credit union system on possible actions to further pursue this topic.

# The Big Picture

All credit unions practice CSR—it is core to their DNA and their reason for being. Many credit unions now also proactively manage this aspect of their business, in order to achieve greater impact, attract members and employees, reduce costs, grow revenues, and build their brand and competitive differentiation. They build CSR strategies and business models into their corporate plans and remuneration systems. To do so they set goals, targets, and metrics to guide and monitor performance and achieve results.

This trend in credit union management is mirrored in the broader economy, with more conventional businesses adopting and advancing CSR measures. Many general academic and financial studies point to the business case for CSR. For example, recent research reveals that companies with robust sustainability (CSR) practices demonstrate better operational performance and positive stock price performance.[5] Their sustainability investments are shareholder-value enhancing and not value destroying.[6]

In addition to these generic studies, sectoral research on the financial benefits of value-based banking was conducted recently by the Global Alliance for Banking on Values (GABV). GABV is a network of 27 banks and banking cooperatives (including three Canadian credit unions and five small US banking institutions) holding a combined US$100 billion in assets under management; it was founded in 2009 with the goal of using finance to deliver sustainable development for underserved people and communities and the environment. Their 2014 research shows that financial institutions with business models based on the GABV Principles of Sustainable Banking produce higher financial returns than the largest banks in the world. According to GABV, "these sustainability focused banks, with a social, environmental and economic triple bottom line at the core of their business models, deliver these results while continuing to be focused on meeting the needs of their clients through lending and deposit products."[7]

So, both generic and sector-specific research demonstrates the business and growth benefits of CSR. The focus of this study is not, however, on how CSR can *create value* for the credit union but on how it can *protect value*.

## *Bank Approaches to CSR as a Risk Mitigation Tool*

The CSR reports of TD, RBC, JPMorgan Chase, and Bank of America reveal that these banks are evolving their CSR strategies to address and improve social, economic, and environmental conditions in their markets and the social and environmental performance of their customers. None of the banks, however, include CSR issues in their formal risk management program. That said, their CSR disclosures suggest that they are beginning to understand the degree to which community economic, social, and environmental health improves their balance sheets and risk profile. For some, their risk management frameworks identify a new class of risks, variously called new, emerging, or evolving risks. These stand apart from their conventional risk disclosures, revealing the emergent nature of these topics. Examples of their CSR–risk connections include:

- Acknowledgment that investments in employee health and wellness reduce operational expenses.
- Awareness that positive and inclusive work environments help retain talented staff and deliver superior customer service.
- Knowledge of the risk climate change poses to their business, their clients, and the communities in which they operate and acceptance of responsibility to mitigate climate change by financing the transition from high-carbon to low-carbon sources of energy.
- Assessing portfolio exposure to carbon and water risks.

As banks, along with credit unions, traverse the CSR path, they, too, will likely evolve their risk programs to more formally bring traditional and CSR risk programs together. Today they are positioned right next to each other. It is a short conceptual leap to imagine them being combined, and the business and CSR benefits that might result if they were joined up.

Against this backdrop, the report will now review possible answers to the question: Can CSR be a useful risk mitigation tool?

# CSR as a Risk Mitigation Tool: Research Findings

While none of the credit unions treat their CSR investments as an explicit and intentional risk mitigation strategy, they readily agree that tying CSR to risk in this way makes intuitive sense.

> *"Top risk benefits: Cost-effective operations, mitigating credit losses, differentiation in our strategic outlook."*
>
> —VANCITY CREDIT UNION FINANCIAL EXECUTIVE

However, credit union leaders also believe the relationship is largely intangible and hypothetical, since the metrics to validate the intuitive claims are unavailable and there are many externalities that make causation and correlation conclusions difficult.

With this disclaimer in mind, the following is a summary of their comments, including success stories and metrics where they exist. It reviews one risk at a time, summing up credit union views on the role CSR can play to mitigate, reduce, or pivot the risk.

## Credit Risk

Generally speaking, credit unions agree that their CSR investments contribute to community resilience by strengthening local economies, improving member financial capacity, and fostering financial inclusion. Through their focus on responsible credit use and savings, financial literacy initiatives can enhance the creditworthiness of members and those with financial barriers. Economic-development-oriented CSR and financial literacy/capacity building in communities improve credit risk if credit unions can successfully achieve results in these areas.

Credit unions with CSR lending portfolios find that their "community impact" book of business has equal or lower delinquency rates compared to their conventional commercial loans. As an example, for three years Vancity has tracked the delinquency performance of their impact portfolio versus their regular commercial portfolio. They have found that their impact loans perform better than their conventional loans. Another example cited from third-party research is that green building loans are better credit risks because of their attraction to tenants—they lease out faster and at higher rates.[8]

> *"We should bust the myth for those who think a CSR lending portfolio is riskier—even if it's the same risk, you can get all these benefits which you can capture. Tying it to risk mitigation is helpful for those who think impact lending is riskier, because it can be demonstrated it is not riskier."*
>
> —VANCITY CREDIT UNION FINANCIAL EXECUTIVE

By focusing on member well-being first and thinking long term, credit unions invest in efforts to protect members from financial difficulty. By embedding CSR in member advice and service, credit union staff proactively identify and support members at risk of unemployment, falling real estate prices, rising interest rates, etc. The credit crunch from the global financial crisis is often referenced to bolster this idea. Many credit unions adjusted their repayment policies for members in hardship during this time, resulting in fewer foreclosures. In so doing, credit unions further protected their assets by maintaining the property value of houses in the area.

Additional, albeit hypothetical, proof points that CSR can help mitigate credit risk include:

#### Environmental Examples

- Lenders possessing broad CSR mind-sets help business members identify and address operational risks from environmental trends (e.g., business disruption from climate change impacts, transition to a low carbon economy, resource and water scarcity). This value-added advice helps improve credit risk arising from business members being unprepared for the impacts of these trends.
- Supporting business and retail members to improve their environmental practices makes members financially stronger and strengthens the credit union portfolio.
- Supporting business and retail members to anticipate and prepare for the physical and business disruption impacts of climate change may reduce defaults in the commercial and retail lending portfolios. Mortgage portfolios in geographical areas at high risk of extreme weather, flooding, rising sea levels, drought, or wildfires, for instance, may face devaluation risks and have higher payment defaults; a credit union's CSR can help mitigate this.
- Financing the transition to a low-carbon economy by, for example, lending to the renewable energy and clean technology sectors can reduce the carbon intensity of the credit union's business portfolio and enhance portfolio diversification.

- If members are supported to invest in their homes (e.g., insulation, eco-friendly renovations), the homes may hold their value longer, improving the assets credit unions use as collateral.

### Social Examples

- Grants and donations can strengthen the community, build community self-sufficiency, reduce crime and vandalism, and create stronger mortgages in the area.
- Banking the unbanked and financially excluded can enhance community resiliency in the long term, especially if pursued in collaboration with community, government, and other partners. A healthier community should result in fewer loan defaults.
- Banking diverse businesses such as those owned by new immigrants, women, Aboriginal entrepreneurs, etc., diversifies the business portfolio, creating resiliency by spreading risks over different groups of entrepreneurs. Third-party research shows that diverse business owners work hard, don't overextend their credit, and have lower bankruptcy rates.
- Financial literacy programs can help members better manage their finances and the volatility of market prices.

> "*When we invest in high-profile CSR projects which our members value, when members are behind on their loans they don't just up and walk. They don't want to hurt the credit union because we are so invested in our community. This builds our relationship with the member and the loss risk decreases because of this relationship.*"
>
> —AFFINITY PLUS FEDERAL CREDIT UNION EXECUTIVE

## Liquidity Risk

Credit unions intuitively perceive a connection between good CSR and liquidity risk, though the connection depends on membership awareness and understanding of the credit union's CSR. If the credit union's CSR business model is visible to members (as credit unions create more social impact through CSR and more awareness through CSR marketing) this becomes a factor in member loyalty. Liquidity risk can be reduced if members understand the flow of their money and how it is being put to use: deposits become less price sensitive and more loyal and long-term. Effective, sustained, and valued CSR can help build a stable core deposit base. Further, since credits unions are more reliant on members to fund member borrowings compared to banks, CSR can be a critical tool to reduce the liquidity risk of this business model. The greater degree of member-funded core deposits funding loans, compared to banks, which rely on short-term financing, gives credit unions more control.

Additional points raised include:

- In times of crisis, credit unions have stronger, more trusted relationships with members, making them less likely to pull out their money; they are more likely to stick with the credit union.
- Millennials prefer to do business with businesses that have a social purpose when choices are available. CSR can be a differentiator on liquidity, especially given that young people are more mobile.
- For wealth products, CSR-oriented credit unions offer financial planning and advice to members to enhance their financial literacy and well-being and educate members about the benefits of socially responsible investment.

> *"Depositors will be more loyal and less likely to switch based on price as a result of a credit union's CSR. The more social-purpose-driven your organization is, the more it is an acquisition and loyalty strategy—you would assume it would impact your core deposit base and your liquidity would be enhanced. The number one capital you want to attract is member deposits. This theoretical hypothesis is more likely if members are aware of how the flow of money is used. It is dependent on an investment in educating the member. If you don't bother to tell anyone, there won't be any loyalty."*
>
> —SERVUS CREDIT UNION EXECUTIVE

## Operational Risk

CSR has the potential to mitigate operational risk and reduce operational cost pressures through four channels.

### Employee Attraction and Engagement

Competition for qualified employees is intense within the financial services industry and from nonfinancial industries looking to recruit, with looming labor market shortages potentially affecting a credit union's ability to achieve its operational goals. CSR can help alleviate this risk. A growing body of evidence suggests that job seekers prefer to work for organizations with CSR practices.[9] CSR can also help reduce employee relations and turnover risk while building member confidence through solid employee tenure. Credit unions can attract a different type of talent by virtue of their CSR, talent that is highly motivated and engaged. Employee resilience can be fostered through the alignment with employee values. While corroborating data are lacking, it is believed that credit unions with effective CSR have higher employee engagement and less churn, saving turnover and recruitment expenses. Third-party research supports this view, with proof that companies with strong CSR programs enjoy higher employee morale and loyalty.[10]

> *"I think this is absolutely true based on feedback from the head of recruitment. More and more candidates are asking what our CSR and volunteering programs and support for the community are all about—they are making choices in part based on that."*
>
> —SERVUS CREDIT UNION MANAGER

> *"Our CSR investments help us retain staff. By having solid tenure you build members' confidence in the organization. If you lose employees you lose institutional knowledge—you do things a lot less effectively."*
>
> —AFFINITY PLUS FEDERAL CREDIT UNION MANAGER

A strong internal CSR culture is important—people have to feel respected, valued, and "on purpose." If this exists, employees will be more productive and the credit union can recruit more talent. Engaging employees on CSR can help with change management and get the credit union through good and bad times; employees will be more open to change and more trusting of decisions. Positive and inclusive work environments allow credit unions to retain the talented people they hire. Employees who feel valued are highly motivated to deliver the best service to members.

> *"Being a socially responsible employer can reduce staff fatigue, attract and engage employees, and help us represent our community. This helps us manage our risks and improve our performance."*
>
> —AFFINITY PLUS CREDIT UNION MANAGER

Healthy, engaged employees reduce operational risk because they are more focused on their job, make fewer errors, and are less likely to do something unethical. Holistic wellness programs positively impact employee engagement and satisfaction. By taking steps to improve employee health and wellness, credit unions can reduce health care costs. Investing in employee financial health and retirement readiness will result in stronger financial results for the credit union.

## CSR Culture Can Improve Employee Engagement and Financial Results

First Tech Federal Credit Union believes there is a direct correlation between credit union business results and employee engagement, the latter being influenced by a strong CSR culture. The credit union closely monitors employee sentiment and participation in credit-union-sponsored employee programs. Employee satisfaction and engagement measures as well as employees' community service hours appear on the corporate performance dashboard along with loan growth, ROA, and efficiency metrics. In 2014, the credit union delivered record financial results with a 12.38% increase in assets, 27.85% loan growth, and a 0.53 delinquency ratio while seeing material increases in employee engagement and satisfaction scores, including a 62% increase in employee community service hours compared to 2013.

### Environmental Footprint Reduction

Credit unions that reduce their environmental footprint through CSR measures can reduce operating expenses and decrease pressure on the operating expense ratio. By lowering their energy use and greenhouse gas emissions from buildings, branches, and fleets, credit unions can reduce their risk of exposure to anticipated carbon pricing. Additionally, depending on where they are located, credit union operations (real estate, branches, fleets, etc.) may be exposed to risks associated with the physical impacts of climate change. CSR can help credit unions mitigate and adapt to climate change impacts and reduce physical impacts from extreme weather events, floods, rising sea levels, droughts, wildfires, etc.

> *"If you take a sustainability look at your value chain right from suppliers to members, there are many opportunities to be more efficient in the way you run your business. From the energy consumed to the way you have meetings and travel—all of those processes from a sustainability lens can be challenged and improved. If you don't take advantage of this, your efficiency ratio will go up—that is a risk."*
>
> —SERVUS CREDIT UNION MANAGER

### Supplier Risks

Many credit union business partners are an extension of the credit union. Credit union CSR supply chain programs such as sustainable purchasing can help suppliers, vendors, and business partners improve their CSR performance and reduce third-party risk.

### Earned Media

Credit unions find that their CSR attracts favorable media attention. This "earned media" has advertising value, can be assigned a dollar value, and, if desired, can be used to offset advertising budgets, reducing operating costs.

## Reputation Risk

Credit unions manage reputation risk by taking social, environmental, and economic (CSR) considerations into account in their decisions, including account openings (who they conduct business with) and product and service innovation. Additionally, through CSR a credit union creates trust and goodwill in the community and among members—this can help the credit union weather storms (e.g., a member data breach). Credit unions that build CSR into their business models, products, and services attract members and grow their business. Credit unions that finance businesses that generate social and environmental benefits can enhance their reputation and brand and further mitigate reputation risk.

> *"Doing the things that make you a good corporation builds respect and trust among those that deal with you. If they believe the organization is doing the right thing, they will be willing to give a little more latitude if something bumps up on the radar, versus an organization that has no reputational collateral."*
>
> —ASSINIBOINE CREDIT UNION EXECUTIVE

## *CSR Investments Build Brand, Reduce Reputation Risk*

Redwood Credit Union has built reputation capital with its members and community over many years, as shown by brand research conducted over 2013–14 in which members and nonmembers qualitatively and quantitatively identified "commitment to community" as a key attribute. The credit union's brand promise as defined by members, "We love to help you succeed," reveals the sweet spot it occupies in the minds of its top stakeholders. This "love brand" is a key component of the credit union's high Net Promoter Score of 74 compared to the industry average of 50.

The credit union's mission—which it defines as passionately serving the best interests of members, employees, and communities—has been core to its CSR and building its reputational strength. Not only does it reduce reputational risks, but it creates reputation-building opportunities, attracting unique and high-profile partnerships such as that with the state senator when the Californian Lake County wildfires broke out in September 2015. Together they raised over $2.5 million for fire relief efforts from over 12,000 donors, which is designated for community rebuilding and economic recovery projects.

## Strategic Risk

CSR can be an aid to strategic risk management in a number of ways. First, when developing business strategies CSR-minded credit unions consider potential impacts on stakeholders and social and environmental trends that pose a risk to strategy execution. In doing so, credit unions can better anticipate, avoid, and otherwise address threats to strategy implementation. By applying a CSR lens to their corporate strategies and alliances, credit unions can remain relevant to current and future members and mitigate reputation risk.

> *"CSR is about taking a long-term approach for members, communities, and your organization. If you have a long-term, 10–20 year CSR vision it will guide strategic choices in a different way. CSR enables you to make the right decisions for long-term sustainability."*
>
> —ASSINIBOINE CREDIT UNION MANAGER

> *"CSR helps you broaden your perspective. If you just focus on economic and financial metrics, you might miss out on something that will have an impact on your profitability because you are not looking broadly enough. Climate change is an example of this."*
>
> —SERVUS CREDIT UNION MANAGER

Stakeholder engagement is an important CSR focus. In addition to taking stakeholder interests into account in strategy design and implementation, credit unions that consult and engage stakeholders such as employees, members, community organizations, policymakers, suppliers, and others stay abreast of their emerging concerns and priorities. This makes the credit union better informed about and attuned to stakeholder expectations and better positioned for effective decision making.

CSR-oriented product innovation also supports strategic risk management. CSR-themed products can mitigate the risk of failing to understand and appropriately leverage environmental and social trends to meet new member demands for products and services. An environmental example is the shift to a low-carbon and zero-waste economy. This economic trend will generate demand for green products and services such as renewable energy and circular economy[11] financing. A social example is predatory lending alternatives, such as Vancity's Fast and Fair loan, which has no fees, low borrowing costs, and same-day service. Financial institutions that create financial options to advance a low-carbon and inclusive economy may enjoy a strategic, competitive advantage in the marketplace and mitigate the risk of losing business to competitors.

As these examples show, given the highly commoditized nature of most financial products, credit unions that harness CSR to distinguish themselves in the marketplace are expected to gain competitive advantage. It is generally believed that a credit union's CSR investments help attract members (especially Millennials, who value social engagement), build loyalty, and improve member retention and share of wallet. Credit unions leveraging CSR to generate a pipeline of new members mitigate the risk of declining member acquisition. This can improve strategic prospects.

> *"Our STEM [science, technology, engineering, and math] charitable investments and partnerships are designed to improve the viability of the tech sector and grow the tech industry. This improves our strategic risk, as we are helping build the technology sector of the future. Our commitment to growing future tech leaders will help ensure a long-term pipeline of potential members to support future growth of our business."*
>
> —AN EXECUTIVE AT FIRST TECH FEDERAL CREDIT UNION, A SEG-BASED CREDIT UNION BASED IN OREGON THAT SERVES TECHNOLOGY-ORIENTED COMPANIES AND THEIR EMPLOYEES ACROSS THE UNITED STATES

Credit unions whose entire business model is based on CSR require CSR success to realize their corporate strategy goals. Assiniboine, Affinity, and Vancity, for example, put member well-being and healthy communities at the center of their business. Their CSR (which they call *values-based banking*) is the foundation of their corporate strategy and culture. See the sidebar for a description of how Vancity's values-based banking business model is driving net member growth.

## Values-Based Banking Attracts and Retains Members

Recent (2013–14) Vancity research reveals that members are more likely to join and stay with the credit union for values-based reasons. Vancity also found that these new members are more likely to be younger—over 40% of new members randomly selected for the survey were 25–34 years old. This is statistically younger than the overall membership. The credit union's ability to retain members improved by 13.5% year over year from 2013 to 2014. The combination of strong new member acquisition and improved retention translated into net member growth of slightly more than 8,000 (1.6%, compared to 1.4% growth in total British Columbia credit union membership). Vancity ended 2014 with 509,008 members. Vancity concludes that "these results and our research suggest that our values-based approach to banking is resonating."[12]

Finally, through CSR-aligned employee diversity and inclusion efforts, credit unions can remain representative of their communities and ensure ongoing relevance to changing member demographics and expectations.

*"Yes, there is a direct association between competitive risk and CSR. However, we don't have the analytics on this. The thinking is more philosophical—that the more in line you are with the values set of your member the greater the likelihood that they will shop with you."*

—SERVUS CREDIT UNION MANAGER

## Regulatory Risk

CSR-focused organizations have cultures that are more likely to avoid regulatory risk. CSR sets the tone in a credit union, helping it to avoid ethical breaches, fines, civil suits, and regulatory actions. As values-based organizations, credit unions operate to standards beyond the legal minimum. Due to their CSR values, credit unions would not try to skirt the rules and risk regulatory penalties. Equally, credit union CSR efforts may help to reduce the number of member concerns and complaints escalated to regulators due to stronger member loyalty.

Credit unions can also avoid regulatory risk associated with anticipated energy efficiency regulations and carbon taxes imposed by governments addressing climate change. By reducing operational energy use and greenhouse gas emissions through CSR programs and helping their members do the same, credit unions can reduce the impacts of potential new regulations in this area.

*"Through CSR it is possible to get in front of the policy train."*

—SERVUS CREDIT UNION MANAGER

The positive social, economic, and environmental benefits generated by credit unions could be a public policy rationale for favorable regulatory treatment. Credit unions generate benefits that improve social, economic, and environmental conditions, which could be valued by legislators and help build a more understanding, open, and forgiving relationship. The more credit unions demonstrate their tangible, measured, positive CSR impacts, the better regulators can understand their business model and the more likely governments will be to give credit unions preferred partner status.

*"Sharing CSR impacts and results with lawmakers can be an influential tool."*

—FIRST TECH FEDERAL CREDIT UNION EXECUTIVE

*"In our marketplace, governments ask us to partner on programs, such as the foreign credential recognition program. We were sought out by the province and the federal government because they knew we were interested and good at this."*

—ASSINIBOINE CREDIT UNION MANAGER

> *"I think it is being more intentional about connecting how our values-based banking business model reduces our risk. Having more facts around the CSR–risk connection helps me get my points across when I am talking with the regulator."*
>
> —VANCITY CREDIT UNION CREDIT EXECUTIVE

## Systemic Risk

By working together and in collaboration with members, industry, and government, credit unions can mitigate systemic risks such as rising household indebtedness, income inequality, unfunded retirements, low levels of financial literacy, climate change impacts (e.g., extreme weather events, rising sea levels, droughts, floods, wildfires), the transition to a low-carbon economy, labor market shortages, and demographic change. Through CSR-oriented collaborative mechanisms with other credit unions, the financial sector, the public sector, and others, credit unions can likely reduce the frequency and impact of these risks. If the credit union system picked one of these issues and tackled it for the long-term, it might be possible to move the needle and mitigate the systemic risk arising from the issue.

> *"At a global level, CSR is probably a piece of the systemic risk puzzle. There is something here, especially with respect to helping business members deal with these systemic risks, but I'm not sure of the degree and significance of the activity."*
>
> —ASSINIBOINE CREDIT UNION EXECUTIVE

## Market Risk

By design or default, credit unions invest in the real economy through their lending and investments. Since the majority of their loans are funded by member deposits, potentially attracted by CSR as described earlier in the "Liquidity Risk" section, credit unions have a more stable funding base that is less reliant on external funding sources and external, costlier market prices. Because their success is tied to the real economy, credit unions are more protected from early liquidations, thereby reducing market risk in their growth. Rather, this approach positions credit unions for sustainable growth.

> *"In our values-based banking model, we sustainably grow with our members and our community in pursuit of building healthy communities. The way we grow is lower risk, as our lending assets are made directly to our real economy and we fund this growth through our member deposits. In our funding of growth, we target 80% of our member loans being funded by member deposits. This model for growth would exhibit lower market and liquidity risks as a result. That said, we still have market and liquidity risks*

*that require proactive risk discipline in managing risks; thus, we have contingency funding lines and maintain proactive risk management strategies that are driven to maintain stable earnings."*

—VANCITY CREDIT UNION TREASURY EXECUTIVE

CHAPTER 5

# Recommendations

Here are some ideas for how credit union boards, risk and credit officers, CSR staff, and credit union associations can help credit unions and their communities profit from these findings.

## Credit Union Boards

- Hold a board discussion on the relevance of the findings to your credit union's CSR and risk strategies. Determine if any of these risks have the potential to be mitigated by your CSR model.
    - Assess whether your CSR model needs to be enhanced so it can more effectively contribute to your risk management approach.
    - See if there are two or three areas that resonate with your credit union where there is likely a strong correlation. Conduct research on potential metrics and see if they can be incorporated into your risk management activity. Start to build your metrics in this area so that in three or five years you can measure the effectiveness of CSR as a risk tool.
    - Start where the correlation might be easiest to demonstrate, e.g., operational or credit risk.
- Make sure your CSR purpose and objectives are clear and understood at the enterprise level in order to achieve these benefits. Build CSR into the strategic planning process. Ensure it is comprehensive and holistic in nature and helps your credit union to protect and create value.
- Given the board's mandate for long-term thinking and that these are primarily long-term issues, boards could ask managers how this approach is addressed in business plans and decisions.

## Risk and Credit Officers

- Risk officers can conduct further research into how CSR can be a risk mitigation strategy. Where there are strong correlations, develop and test theories.
- Watch how large banks are building their insights and competencies in this area and how they are using this information. Learn from them and get ahead of them.
- Have joint meetings with CSR, credit, and risk staff to build collective competencies and knowledge about the connection between CSR and risk management. Identify joint projects to test and prove the propositions and develop the fact base.
- Use the report in risk and credit staff training sessions to build understanding, knowledge, and confidence in using CSR as an approach to risk mitigation. By building awareness of these ideas, staff can better incorporate them in their daily work. This can help them understand and enhance the difference between cooperative and traditional financial institutions.
- Develop sustainability stress tests to explore the impact of future environmental and social scenarios on the portfolios and business models of the credit union. Scenarios could cover climate change impacts, rising inequality, water stress, wealth transfer, etc.

> *"For me there is value in understanding and being clear about how values-based banking reduces risk. We need to know what it means from a credit risk perspective. For instance, we are tracking delinquency on businesses that provide environmental services. If we know the delinquency in those areas is good, then why don't we lend more to them? I am reframing how we do portfolio analysis from this perspective."*
>
> —VANCITY CREDIT UNION CREDIT EXECUTIVE

## CSR Staff

- Become familiar with the role CSR can play in mitigating enterprise risk. Hold meetings with risk, credit, and treasury colleagues to identify if and how the connections between risk and CSR can be strengthened and built into the credit union's scorecard and corporate strategy. Quantify your activities so they can more easily be used in risk models.
- Ensure you are measuring the impacts of your CSR efforts so these results can be factored into risk models. The Canadian Credit Union Association has conducted research on this topic.[13]
- Determine if there are ways your credit union's CSR can be enhanced to take advantage of these opportunities. Consider these ideas when setting your CSR strategy.

Understand how social and environmental trends impact your credit union's region, market, and portfolio and can become risks and opportunities for your organization. Make this information available to those setting the credit union's strategic direction.

## Credit Union System

- System organizations (provincial centrals, state leagues, national trade associations) can raise awareness of this approach with credit unions to improve the system's capacity in this area.
- Boards and risk committees of credit union system organizations can review these findings to consider the relevance to their own risk profiles, strategies, and business plans. CSR could be a strategy for addressing risks that centrals face.
- System organizations can help credit unions test some of these assumptions by creating a framework for data collection on one or two top opportunities. For example, one or two standard metrics could be developed for credit union tracking and benchmarking, such as including a common CSR question in employee surveys to measure the benefits of employee engagement, or metrics to measure portfolio carbon risks, the business benefits of financial literacy programs, or delinquency rates of CSR impact loans, to name a few.
- System organizations can help the credit union system tackle systemic and regulatory issues by further understanding how collective, systemwide CSR efforts can mitigate these risks to credit union success. For example, by working together and with other stakeholders such as governments, members, and civil society, credit unions might improve systemic risks such as rising household debt, unfunded retirements, the physical and regulatory impacts of climate change, and financial exclusion. If these systemic risks can be improved through collaboration, centrals may be able to identify one or more of these issues to tackle through their strategic planning.

# CSR Sampler

A sampling of CSR best practices for credit unions is listed in Figure 2. They can be used as a checklist for credit unions that would like to expand their definition and understanding of CSR. They are derived from a credit union social purpose assessment tool available at www.libro.ca/Community/Documents/Social-Purpose-Assessment-Tool.pdf.

FIGURE 2

SAMPLE CSR BEST PRACTICES

*Governance: We embed CSR into our governance and management systems.* Examples:

1. CSR in mission, vision, values, corporate strategy, balanced scorecard, brand
2. CSR in human resource practices
3. CSR in budgeting, project approvals, decision making, strategic planning, innovation processes, etc.
4. CSR oversight by board of directors; CSR reporting
5. CSR in lending, credit, and account opening procedures

*Members: We engage our members in our CSR efforts, we enable their financial resilience, and we use our products and services to foster sustainable growth.* Examples:

1. Support member long-term financial health (financial literacy, etc.)
2. Finance and support development and growth of CSR-oriented markets and organizations (e.g., local food, social enterprises, renewable energy)
3. Bank member segments that generate social or environmental benefits (e.g., underserved/underbanked groups)
4. Offer members CSR-oriented products and services that improve social and environmental conditions
5. Engage members in CSR efforts (e.g., CSR-type deposits, mortgages and loans, impact investments, donations, volunteering, buy local programs)
6. Assess loans and investments for environmental and social risks at the portfolio level; use CSR programs to mitigate risks

*Communities: We engage our communities in our CSR efforts, we enable their resilience, and we use our branches, products, and services to foster sustainable growth.* Examples:

1. Community strategy includes a range of funding options from grants to loans to equity investments, pooled funds, etc.
2. Community strategy includes a range of financial and nonfinancial resources, products, and services—harnessing banking core competencies and expertise
3. Measures are pursued to build financial capacity of communities, enhance savings and reduce over-debt levels, and promote sustainable consumption
4. Multi-stakeholder collaboration and government public policy advocacy is pursued to improve community conditions
5. Business members are helped to address business impacts of social trends influencing the community (e.g., aging, out-migration, immigration)

*Environment: We reduce our direct and indirect environmental impacts and foster a sustainable economy.* Examples:

1. Goals, targets, and measures to reduce direct environmental impacts (e.g., energy and greenhouse gas reduction, waste reduction, paper use reduction, renewable energy, green buildings/branches, employee commuting, green meetings, green IT)
2. Provide members with financial products and services to promote environmentally sustainable choices (e.g., green business/housing/car/renovation loans; finance environmental businesses such as renewable energy, clean technology, and businesses producing green products and services)
3. Members and other stakeholders are encouraged to make positive environmental choices
4. Understand and reduce the greenhouse gas emissions and waste and water impacts of lending and investment portfolio
5. Business members are helped to address business impacts of environmental trends influencing the community/region (e.g., rising energy costs, climate change impacts, water scarcity, government environmental regulation)
6. Multi-stakeholder collaboration and government public policy advocacy is pursued to improve the environment

*(continued)*

FIGURE 2

## SAMPLE CSR BEST PRACTICES *(CONTINUED)*

*Suppliers and business partners: We engage our suppliers and business partners in our CSR efforts.* Examples:

1. Buy green/social products from environmentally and socially responsible suppliers
2. Buy from local, cooperative, diverse (e.g., immigrant, Aboriginal owned, etc.) suppliers and social enterprises
3. Collaborate with suppliers to collectively improve social and environmental impacts of the credit union's supply chain
4. Collaborate with other buyers in social/green/local procurement projects
5. Influence CSR standards and performance of industry sectors and professional associations

*Cooperatives: We support the growth of a strong and resilient cooperative sector.* Examples:

1. Member and employee training and communications on the value of the cooperative model, behavior, and practices
2. Cooperative sector strategy includes goals and targets to increase co-op lending, sourcing, partnering, and joint venturing
3. Cooperative strategy includes measures to support emergent cooperative and collaborative models such as crowdfunding, sharing of goods, etc.
4. Cooperation, cooperative values, and cooperative business models are promoted to stakeholders and measures pursued to grow a cooperative, collaborative, and sharing economy
5. Lead or join collaborations with the credit union and cooperative sector to improve the sector's CSR and cooperative performance and to tackle common CSR priorities together

# Endnotes


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# List of Figures

# About the Author

## Coro Strandberg

**President, Strandberg Consulting**

Coro Strandberg, president of Strandberg Consulting, is a leading sustainability and corporate responsibility consultant, with over 25 years of experience advising credit unions and other companies on the design and implementation of community investment, CSR, and social purpose business models and strategies. A trusted authority on credit union social responsibility, Coro was hired by the Canadian Credit Union Association (CCUA) to produce guides on the credit union CSR business case, responsible procurement, CSR governance and management, CSR metrics and reporting, and how to develop a CSR strategy, available at CCUA's CSR Information Hub. Coro conducts CSR training for credit union boards and managers for CUSource and others. As a director and then chair of Vancity Credit Union from 1988 to 2000 Coro contributed to Vancity's evolution as a values-based banking leader.

Coro also advises cooperatives, companies, governments, and industry associations on strategies to embed sustainability in business models, enterprise risk management, functions, roles, decisions, sectors, and supply chains. She regularly publishes blogs, articles, research, tools, and guides on sustainability and CSR leadership on her website at www.corostrandberg.com. Recently Canadian Business for Social Responsibility hired Coro to write a guide on the new global standard in CSR leadership in business: the Transformational Company. She is a frequent public speaker on trends and the future of corporate responsibility. Recognizing Coro's deep expertise in CSR and corporate sustainability, the Canadian Government's Office of the Auditor General appointed her to its Sustainability Committee to provide advice on measures to monitor the federal government's progress on fulfilling its sustainable development commitments.

Coro was named the top CSR consultant in 2015 by Canada's Clean50 for her leadership and impact in sustainability consulting in Canada. She lives in a LEED Gold certified home, which she built with her partner in Burnaby, British Columbia.

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Filene Research Institute is an independent, consumer finance think and do tank. We are dedicated to scientific and thoughtful analysis about issues affecting the future of credit unions, retail banking, and cooperative finance.

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**—Edward A. Filene**

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Publication #398 (3/16)