Third Side Strategies

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Mitigating the Ultimate Systemic Risk:

Key Questions Investors Should be Asking about Public Affairs Governance Right Now

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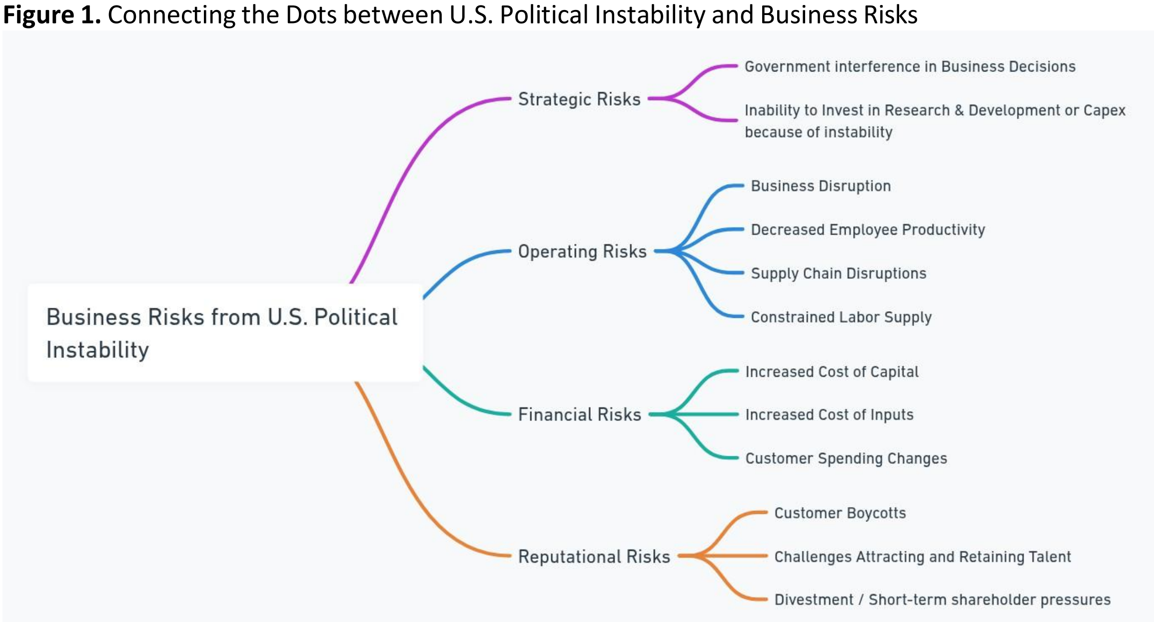
As investors increasingly focus on systemic risks, few risks are as consequential as the weakening of democratic institutions and the rule of law. Companies are facing once-in-a-generation operational and strategic challenges—navigating AI, workforce shifts, energy transitions, and stakeholder pressures, in an increasingly chaotic political environment. Without a stable, functioning government, challenges like these are almost impossible to manage effectively, and the foundation for innovation and long-term value creation begins to crack.

The result: companies face growing exposure to financial, operational, and reputational risks (see Figure 1), with little clarity on when or how to engage.

Figure 1. Connecting the Dots between U.S. Political Instability and Business Risks



As an investor, it can be difficult to translate the risks from weakening rule of law into concrete actions companies can take to mitigate those risks. Focusing on public affairs governance – how companies make decisions about whether and when to engage in the public sphere, can be one helpful lens.

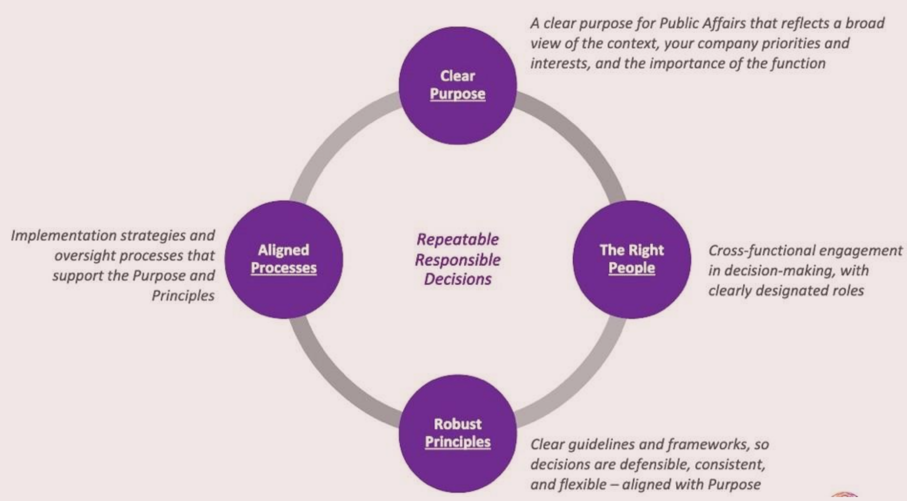
Why Focus on Public Affairs Governance?

Making decisions about corporate engagement in the public sphere can feel like walking a tightrope for many companies right now, and investors need to understand how companies are making and managing those decisions. All of this raises the bar for public affairs, understood broadly:

"Public affairs is an organization's strategy to monitor, manage and impact its business environment. It integrates government affairs; advocacy; communications; environmental, social and corporate governance; and issues management to influence public policy, build a strong brand and find common ground with stakeholders." - The Public Affairs Council

We believe that applying Corporate Political Responsibility (CPR) Governance, which is a set of best practices that include the key elements in Figure 2 to public affairs decisions, reduces risk, enables long-term value creation, and supports achieving business purpose and fiduciary duty.

Figure 2. CPR Governance as Repeatable Responsible Public Affairs Decision-making



It's time for investors to ask sharper questions—of companies and of themselves. Asking companies questions about CPR Governance helps investors in two ways: (i) it prompts companies to think more concretely about their public affairs practices and strengthen any areas of weakness highlighted by the questions, and (ii) provides investors with the information needed to more effectively manage this systemic risk across their portfolio.

Questions to Companies

Whether managing assets internally or through an investment manager, an investor's due diligence should include questions about how the companies in which they are investing in think about and manage public affairs. Questions to ask include:

Issue Prioritization & Strategic Alignment

1. How are key public affairs decisions made?
   - Which internal business functions are involved in those decisions?
   - How are issues prioritized and linked to strategy? Describe some examples of an issue prioritized for engagement and one that was not.
   - How are tradeoffs between competing policy priorities, company commitments, and stakeholder interests managed?
2. Is there a formal public affairs engagement policy? If no, is the company willing to develop a policy in the next year?
3. Does the company follow any international standards, industry guidelines, reporting frameworks, or initiatives on political spending/public affairs engagement? If so, which ones?

Governance & Oversight

4. What is the Board's role in overseeing public affairs activities?
   - Which public affairs activities are reported to the Board and how often?
   - Which activities require Board approval?
   - Are decisions about when Board approval is required based on materiality? How often does the Board revisit what is material in the current climate?
5. Are systems in place to track and align public affairs activities with other company commitments (community, net zero, DEI, etc.)?
6. What information about public affairs activities is reported to investors and how frequently? What information is reported publicly and how frequently?
7. Has the company received shareholder proposals related to political or social engagement? If so, how were the proposals addressed? Please provide some examples.
8. Does the company monitor the political spending/engagement of any trade association of which it is a member? If not, will it consider doing so in the future? If yes, how does the company deal with misalignment between its own public affairs priorities and the positions taken by a trade association?

Questions for Investors

Just as companies face competing pressures and new risks amid political instability, investors — accountable to their own beneficiaries — should also assess their own public affairs governance in this critical moment. Some questions to consider are:

Investment Management

1. Does your Investment Policy Statement (IPS) currently account for political/public affairs risks?
    - Are portfolio exposures aligned with your values and risk priorities?
    - Do you assess potential conflicts in your portfolio with your public commitments (i.e., to integrate ESG factors)?
    - Is there a defined percentage of misalignment permitted?
    - Does the IPS consider portfolio-level tradeoffs between policy needs of different sectors?
2. Do you have a proxy voting policy that includes direction on how to vote on proposals regarding public affairs governance/political risk?
    - How are conflicts handled – engagement or reallocation? Which factors are considered?
3. How do you monitor and evaluate the companies in your portfolio for public affairs governance? Provide examples.

Governance & Oversight

4. Does the Investment Committee assess public affairs risks?
    - Does your investment committee have the expertise to evaluate public affairs risks across your portfolio?
    - What information regarding public affairs risks gets reported to the Investment Committee and how frequently?
    - What public affairs decisions require approval from the Investment Committee?
5. Do the investment and risk teams (or your investment manager) have the expertise to evaluate a company's public affairs governance, as well as a portfolio-level review of the same?
6. Do you have a public affairs governance policy regarding how you manage public affairs decisions and report to your beneficiaries? If not, are you willing to implement one over the next year?
7. Do your investment management agreements or side letters acknowledge the materiality of public affairs governance? Do they provide direction on proxy voting for proposals related to political spending and public affairs governance?

Resources to Help

Third Side Strategies is here to help. Visit The CPR Hub for a dynamic set of practical resources to support you where you are. Whether new to thinking about this, or knee-deep in examining how public affairs governance may impact your portfolio, we have resources to support you and help craft a customized approach that fits your situation.