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The Climate Custodians

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June 22, 2016

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Introduction

Can custody banks become key players in climate change? Custody banks joining the battle against climate change will signal a significant shift in governance ideology for this highly regulated industry so critical to the global financial system. While global custody banks provide the unseen but essential support system that ensures the proper functioning of the capital markets, they have great untapped potential to become change-makers in climate change.

This paper expands on our idea of the “Climate Custodians” first presented in the [MIT Sloan Management Review](#)¹ within the governance context of the “[Statement of Significant Audiences and Materiality](#) (The Statement)”² for these subsidiaries of large bank holding companies. By focusing on the Big Three global custody banks — State Street, BNY Mellon, and JPMorgan Chase — we make the case for large custody banks assuming the role of climate custodians. In this role, these banks would report, among other things, a measure of carbon embedded within their institutional clients’ assets under custody to help clients understand the climate risk in their portfolios. This paper has six parts. We first review the role of custody banks in the financial system, including the practical realities resulting from market share concentration. Second, we examine the unusual case of significant audiences being required by regulators. In Part III we look at the role custody banks could play in addressing climate change, within existing regulations and following evolving sustainability accounting standards. Part IV evaluates the corporate governance documents of the Big Three custody banks and contrasts their existing governance disclosures with the governance requirements of the banks’ regulators. We follow in Part V by applying our

prior research on director fiduciary duty to the climate role of custody banks and suggest The Statement as a way to address our findings on these banks' governance shortfalls. We conclude with a call for research into changes in the governance disclosures of custody banks and suggest The Statement not only as a tool for bringing custody banks into regulatory compliance, but also as a way to set up a line of defense against bank-holding company short termism. Whether custody banks adopt the climate custodian role depends not on regulatory change, but simply on the will of the boards that govern them.

I. The Role of Custody Banks in the Financial System

Custody banks provide payments and transactions settlement, safekeeping, and reporting of customers' marketable securities and cash,³ enabling liquid securities markets around the world. Custody banks are the hidden plumbing fundamental to the functioning of the capital markets. Securities and currency trading may be where the exciting action and media coverage are, but without custody banks there would be virtually no trading. These banks have no trading decision rights over their custody customers' assets, and take direction from clients, regulators, and other claimants. In Q3 2015, three banks — State Street, BNY Mellon, and JPMorgan Chase — held \$75.5 trillion in custody assets spread across a global interoperable network of sub-custodian banks, which represent nearly two-thirds of tradeable global assets⁴. In comparison, the four largest central banks — The Federal Reserve (United States), the European Central Bank, the Bank of Japan, and the Peoples Bank of China — held a combined \$15.6 trillion in assets.⁵ Because of the concentration of the majority of the custody industry's assets into these Big Three global custody banks, combined with their sheer size, they are systemically important to the liquidity and safekeeping of the global economy. Both the custody banks and their largest clients and counterparties (asset managers, pension funds, non-custody banks, securities trading entities, and large asset owners) are highly regulated. The practical reality of this industry's asset concentration is that the United States' regulators of these three United States banks are the de facto regulators of the global custody banking system.

There is growing recognition by major players in the global political and financial systems — such as The [Financial Stability Board's industry-led disclosure task force on climate-](#)

[related financial risks](#) , the two big United States pension funds of [CalPERS and CALSTRS](#), the [Portfolio Decarbonization Project](#)” assembled by the Swedish pension fund AP4 and French asset manager Amundi with committed assets of \$600 billion, and Ceres’ [Investor Network on Climate Risk](#) with \$13 trillion in assets —that reversing the trend in climate change is key to the long-term survival of mankind. These players are leading a growing conversation about the role large corporations can play in addressing the perils of climate change and about how institutional investors and regulators can support these efforts. The role of global custody banks, however, has been missing from the conversation. Their absence from the narrative isn’t surprising, since few outside the financial industry have heard of custody banks, let alone, know what they do.

This paper makes the case that for large, global custody banks taking on the role of climate custodian is consistent with — and even required by — the regulations under which they operate. However, the decision of whether or not to take on this role rests squarely on the shoulders of the boards that govern them.

II. The Required Significant Audiences of Custody Banks

In the paper “[Materiality in Corporate Governance: The Statement of Significant Audiences and Materiality](#),”⁶ we asserted that “shareholder primacy” is an ideology, not a law.⁷

Corporate boards have the option to consider other stakeholders and many do. In that paper, we suggested that boards make their forward-looking point of view clear on which of the company’s stakeholders are most relevant to value-creation by publishing a short annual “Statement of Significant Audiences and Materiality.”⁸ In the specific case of the Big Three global custody banks, however, directors’ options to designate significant audiences are substantially limited by their regulator. In this section we will detail the composite regulatory picture that requires eight significant audiences to be considered by directors of these global custody banks, including the requirement for strict prioritization of the top three audiences. As we will show, each shareholder of the Big Three can be ranked no higher than third among the eight required significant audiences. Also included in these eight required audiences are “the global community” and “the global economy.” Given the planetary breadth of these audiences, we are calling on global custody banks to become

climate custodians for planet Earth. Taking on this role is a necessary, but not by itself sufficient condition for fulfilling their cosmopolitan governance responsibility.

The Big Three custody banks are separate banking subsidiaries of their parent bank holding companies. In addition, they are U.S.-chartered custody banks,⁹ national banks,¹⁰ and large banks,¹¹ classifications that fall under the supervision and regulation of the Department of the Treasury's Office of the Comptroller of the Currency (OCC). Each bank subsidiary is required to have a board of directors separate from the board of their parent holding company.¹² Our research has shown that directors of The Big Three are required by the OCC to consider eight significant audiences in their fiduciary and materiality determination roles: the bank as a separate legal entity, depositors, shareholders, custody counterparties, global sub-custodian banks, regulators, the global community, and the global economy. While directors of these global custody banks are required to consider these specific eight significant audiences, they have the option to consider other significant audiences beyond these eight.¹³ The board of one of the Big Three custody banks does consider one audience beyond the required eight.

Before we detail our composite view of the regulatory requirements underpinning these eight significant audiences, we note that the Big Three are not widely held by many shareholders. In fact, each bank has only one shareholder, which is their respective parent holding company. This important governance qualifier is recognized by the OCC in their regulatory guidance. We also note that by virtue of their national bank charter under the regulatory supervision of the OCC, national banks are essentially "national corporations." Under the federal supremacy clause of the US Constitution, this imposes federally required fiduciary and other duties that override those required by national banks' incorporating state.¹⁴

The OCC requires that a global custody bank put the interests of the bank and of its depositors above those of its shareholder. In the "Duties and Responsibilities of Directors, Comptroller's Handbook," the OCC states that: "The directorate is responsible to its depositors and shareholders for safeguarding their interests through the lawful, informed, efficient, and able administration of the institution."¹⁵ However, the primacy of directors'

duties to the shareholder and depositor audiences is modified in the case of custody banks that are also national banks, and specifically national banks that are subsidiaries of bank holding companies. In “The Director’s Book, The Role of a National Bank Director, Directors Toolkit (National Bank Directors Book),” the OCC says that “Directors of a national bank are accountable not only to their shareholders and depositors but also to their regulators,”¹⁶ The OCC narrows this direction in the section titled “MAINTAIN APPROPRIATE RELATIONSHIPS WITH THE PARENT HOLDING COMPANY AND BANK SUBSIDIARIES ... For its part, the primary duty of the subsidiary bank’s board of directors is to protect the bank.”

Further, “If the [subsidiary bank’s] board is concerned that the holding company is engaging in practices that either may harm the bank or are otherwise inappropriate, the board should notify the holding company and discuss modifications. If the holding company’s board does not respond to the bank’s concerns, the bank’s board should dissent on the record and consider action to protect the bank. The bank’s board should hire an independent legal counsel or accountant if it decides it is necessary. The board also may raise its concerns with bank supervisors.”¹⁷ Underscoring the bank directors’ duty to put the interests of the bank and depositors above those of its holding company shareholder, the OCC goes on to directly address subsidiary bank director liability for failing to do so: “A director’s recorded dissent in the board minutes also may protect that director from some potential liability resulting from the board action.”¹⁸

When the Comptroller’s Handbook’s primary director responsibilities are combined with the National Bank Director’s Book’s primary director responsibilities, it is clear that, in the case of the Big Three, the bank’s board is required to subordinate the interests of the shareholder, aka the holding company, to the interest of the bank itself as a separate legal entity, and to the interest of depositors. Therefore, the duty of a Big Three custody bank director is primarily owed to the bank itself and to depositors, above the duty to the subsidiary bank’s shareholder.¹⁹

In addition to the separate legal entity of the bank itself, bank depositors, and their shareholder holding companies, the OCC also requires directors of large custody banks to consider five other significant audiences within their governance duties: their custody

counterparties, global sub-custodian banks, regulators, the global community,²⁰ and the global economy²¹ as a whole.

Counterparties to the core custody services of settlement, safekeeping, and reporting are audiences embedded in the OCC's definition of a custody bank.²²

Regarding global sub-custodian banks, in the "Custody Services, Comptroller's Handbook," the OCC details thirty-nine instances of "sub-custodian" related to risk, compliance, core custody services, and even a "Global Sub-Custodian Network" section with two "due-diligence" subsections. Given the prominence of the sub-custodian audience in this handbook, we conclude that this audience is one that custody banks directors should be "fully aware of [in] fulfilling their responsibilities."²³

Per the National Bank Director's Book directors of the Big Three global custody banks, as national banks, "are accountable not only to their shareholders and depositors but also to their regulators."²⁴ Therefore, regulators are a required significant audience for the Big Three.

The OCC specifies the directors' duty toward the global community and the global economy audiences by applying the context of their global scope of custody operations, their huge size, and their high degree of industry asset concentration to the requirement that bank directors "ensure that the bank has a beneficial influence on the economy of its community...conducive to well-balanced economic growth."²⁵ In our interpretation of this section in the global custody bank context, "the economy" is about growth and, "the community" is about sustainable growth. A board of the Big Three can take a tangible step toward ensuring sustainable growth by deciding to have their bank become a climate custodian.

III. Custody Banks and Climate Change

The OCC-required eight significant audiences for large custody banks could be aggregated as "everyone on the planet." We acknowledge that the breadth of "everyone on the planet" is in opposition to our call for directors to narrow judgement by selecting only a few significant audiences. However, given the rather unique situation of global custody banks,

with their very high degree of market share concentration and systemic importance (similar to the importance of credit ratings agencies), and that some stakeholder advocacy groups, such as ClientEarth,²⁶ have taken the view that “the planet” is a unique stakeholder, we accept that “the planet” can be a significant audience for custody banks. Further, the universal impact of planetary climate change has been embraced by major players in the global financial system. Hence, we feel it is appropriate to address the significant audience of “the planet” within the governance context of “the Statement.”

Our suggestion that global custody banks assume the climate custodian role may help Big Three directors integrate their consideration of “everyone on the planet” in their board’s materiality determination, strategy, and reporting oversight roles. For the custody and asset management industry, the [Sustainability Accounting Standards Board’s](#) (SASB) provisional materiality standards include a metric — the ratio of “Tons (t) embedded CO₂ / U.S. dollars (\$)”²⁷ — that could be tied to individual and aggregate custody assets. Adding this single climate-custodial metric to the \$75.5 trillion in assets already being tracked by the Big Three would be a small but powerful first step in elevating the Big Three directors’ role of ensuring their banks have a beneficial influence on sustainable growth of the global economy for the global community. When global custody banks begin tracking and reporting embedded carbon as an inherent component of the assets they hold for settlement, safekeeping, and reporting for their institutional custody clients across the planet, custody banks would be taking the first step toward becoming climate custodians. It would also be in their economic self-interest to assume this role, since the fees on which their custody business is based are a function of assets under custody, which are at risk of losing value if climate change goes unchecked.

Beyond the fiduciary fit of the climate custodian role, it would appear from a capabilities point of view, that the Big Three may be well positioned not only to adopt this role, but to become a platform for climate and other environmental, social and governance (ESG) financial reporting innovations. Regarding capabilities, State Street EVP Pat Centanni, a 32-year employee of the bank, says that “many of the financial products and services brought to market by a global custodian bank are, in a practical sense, somewhat ‘open source.’ In our safekeeping, settlement, and recordkeeping roles all these products and services must

be interoperable and capable of exchanging key data with our competitors', clients' and industry utilities' systems, be fully transparent on a real-time basis for regulatory monitoring, and provide an 'open' baseline platform for client and third party service provider innovation. Increasingly, the industry is looking to the custodians for greater analytics to better mine the tremendous amounts of data they process and manage.”²⁸

The open-source business model has a robust track record of generating entirely new industries. Perhaps the highly concentrated global custody bank industry, with its organic open-source attributes, can be an incubator for a new environmental, social, and governance (ESG)-value industry. Taking on the role of climate custodian is a good first step. Once this step is taken, we envision the role evolving into a larger long term ESG custodial role.

IV. The Corporate Governance of Custody Banks

We have examined the corporate governance guidelines and principles published by [State Street](#), [BNY Mellon](#), and [JPMorgan Chase](#) for alignment with the OCC's significant audience requirements for large global custody banks. For all three, publicly available governance guidelines and principles discuss audiences only for the bank holding companies. We found no statements that acknowledge the audiences of their legally distinct subsidiary custody banks. In our examination of these public documents, furthest from the OCC standard is JPMorgan Chase, which states that its directors act “on behalf of the Firm's shareholders”²⁹ in clear contrast to the OCC's guidelines, which specify that the interests of the bank itself and depositors come before shareholders' interests. BNY Mellon is slightly closer to the OCC standard in stating that their directors' “primary responsibility is to oversee the management of the Corporation in the interest of the Corporation and its stockholders.”³⁰ State Street's perspective, on the other hand, is more closely aligned with the OCC's significant audience standard: “State Street's directors, in their role of overseeing the sound management of the Company, have the responsibility to exercise their business judgment in what they believe to be in the best interests of the Company and the shareholders, taking into account the interests of the employees, the customers and the community at large, and in so doing enhancing the long-term value of the Company.”³¹

While State Street is missing four (regulators, custody counterparties, global sub-custodian banks, and the global economy) of the OCC's eight audiences, it does recognize four of them (depositors, shareholders, the community at large, and the bank itself) and adds employees as another audience, and therefore ranks highest on the significant audience scorecard. BNY Mellon recognizes two, and JPMorgan Chase only one.

In these publicly available documents, we can find very little references to, nor identification of, the separate roster of board directors that the custody bank subsidiary of each bank holding company is required to have. We can find no mentions by BNY Mellon of a bank board as a separate entity. JPMorgan Chase, in their 2015 10-K filing, says that "the JPMorgan Chase Bank, N.A. Board of Directors is responsible for the oversight of management of the Bank. The JPMorgan Chase Bank, N.A. Board accomplishes this function acting directly and through the principal standing committees of the Firm's Board of Directors [the parent company board]. Risk oversight on behalf of JPMorgan Chase Bank N.A. is primarily the responsibility of the DRPC [Risk Policy Committee of the Board of Directors] and Audit Committee of the Firm's Board of Directors and, with respect to compensation and other management-related matters, the Compensation & Management Development Committee of the Firm's Board of Directors."³² Therefore it appears that JPMorgan Chase has co-mingled the governance functions of the subsidiary bank's board with those of the parent holding company's board. The OCC requires that these board functions be separate in order to protect the subsidiary bank directors from liability and to help assure that the custody bank fulfills its duty to depositors and to the bank itself above the shareholder, as well as to the global community, the global economy and other significant audiences.

In contrast to JPMorgan's 10-K comments about delegating their bank's governance roles upward to the board of the parent holding company, State Street's Corporate Governance Guidelines state "The Board and its committees may meet simultaneously with the board and committees of the Bank. In determining whether to hold specific meetings, the Boards and the committees of the Corporation and Bank should always act in a manner that they determine to comply with policies of State Street and the Bank with respect to conflict of interests and with applicable laws and regulations."³³ Here State Street appears to

acknowledge that the board of the subsidiary bank and the board of the parent bank have separate roles, that each board may hold separate or simultaneous meetings and, by acknowledging the bank's conflict of interest policies, implies that these two boards may have duties to different sets of audiences. Similar to BNY Mellon and JP Morgan Chase, State Street does not identify the members of the subsidiary bank's board, so we have no idea if the subsidiary bank's board is the same roster as the parent holding company's board or whether the members of the two boards are two different lists of individuals.

V. The “The Statement” for Climate Custodians

Based on our global legal research discussed in our paper “Materiality in Corporate Governance: The Statement of Significant Audiences and Materiality,” boards in every country have the latitude to consider whatever audiences they deem significant as they execute their governance duties. In the United States, these audiences must include shareholders and the separate entity of the corporation. The board can consider other audiences as well. However, there are several exceptions where United States companies' board discretion in the selection of significant audiences is limited by regulation or by case law. The first exception is the sale of “all or substantially all” or a “change of control” sale of the company. This is the widely cited “Revlon case” scenario where the court found that directors had a primary duty to the shareholders above all other stakeholders in realizing the best possible price for the company.³⁴ The second exception is for companies' that are in the “zone of insolvency.” Here directors are required to “owe existing duties to creditors.”³⁵ The Big Three – each with only one shareholder (a parent holding company) and each as a national corporation (which overrides state corporate law) - represents a third exception. As discussed above, OCC regulations require that Big Three directors consider eight significant audiences: the bank itself, bank depositors, their shareholder holding company, their custody counterparties, global sub-custodian banks, regulators, the global community, and the global economy. Directors of the Big three are free to select additional audiences beyond the required eight audiences, and State Street has added employees. However, within these required eight audiences, the OCC requires that the global custody bank subsidiaries place the interest of depositors and the bank itself above

the interest of their parent company shareholder and above the other five required audiences.

In order to aid the boards of the Big Three in disclosing their OCC-required audiences as they carry out their ultimate materiality determination duties, in Appendix A we have drafted a Statement of Significant Audiences and Materiality example template that includes the climate custodian role.

Conclusion

Given that the OCC requires that Big Three boards consider eight significant audiences, yet the Big Three disclose only one, two, or four of the required audiences in their governance disclosures, we call for research into changes in the corporate governance disclosures of custody banks, specifically:

What is the best method for global custody banks to disclose who are the members of the custody bank board?

What separate disclosures should be made by the custody bank board, separate from the holding company board?

What should be disclosed by OCC bank examiners regarding custody bank's compliance with the eight required significant audiences and with the degree of separation between the holding company board and the custody bank board?

Issuing The Statement of Significant Audiences and Materiality that includes the role of climate custodian would help the board set up a line of defense against short-termism by the bank holding company - a line of defense which appears to be required by the OCC. By publishing the bank board's view of significant audiences, global custody banks will not only be acknowledging OCC fiduciary requirements, but will also be laying the value preservation foundation for becoming climate custodians. Given the clarity of a bank board specifying the minimum eight required audiences, the initial step of reporting carbon embedded in assets under custody, and thus becoming a climate custodian, seems to be a logical progression.

In our view, if one of the Big Three becomes a climate custodian, the other two will follow. Who will go first will be a function of each bank's perspective on its fiduciary duty and on its analytical, risk, and operational capabilities. For the sake of "the planet," it is important that one of the Big Three global custody banks be the first to issue The Statement in which it formally declares it is taking on the role of "The Climate Custodian."

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Appendix (A): An Example Template for The Statement for Global Custody Banks

_____ Custody Bank, N. A.

Board's Annual Statement of Significant Audiences and Materiality

The _____ Bank, N.A. exists as an entity separate from its shareholder parent holding company, management, employees, and other stakeholders. As a separate entity, the bank can survive many generations. We, the board of directors, are entrusted with ensuring the long-term health and viability of the bank. We have delegated to our current management team the authority to deploy the corporation's limited capitals (financial, manufactured, human, intellectual, social and relationship, and natural) in the pursuit of our ongoing goal of sustainable value creation in our banking operations and services. It is within this context that the board issues this Annual Statement of Significant Audiences and Materiality in order to give forward-looking guidance not only to management, but also to the providers of financial capital, our employees and all other stakeholders, regarding the audiences we feel are the most significant for the upcoming year, and for the next three to five years.

Our regulators require that our bank depositors and the separate entity of the bank itself are our two most significant audiences, followed by our shareholder bank holding company. We are further required to consider the Bank's custody counterparties, global sub-custodian banks, regulators, the global community, and the global economy as significant audiences for the future sustainability of the Bank. Across these significant audiences, we foresee that climate change issues will likely continue to be material to the Bank's sustainability. Regarding global climate change, we have specifically directed management to report the amount of carbon embedded within our custody assets, and to require the same of our global sub-custodian banks. In doing so, we are adopting the role of climate custodian as an integral part of our global settlement, safekeeping, and reporting role for our institutional custody clients, and for the safekeeping of the planet we all share.

We acknowledge that the Bank has many stakeholders. There are many demands on us to fulfill or to symbolize many roles in our communities, given that our social license to operate is granted by society as a whole, and that our national bank charter is granted by the US Department of the Treasury. While the Bank takes great care in exercising this social license and our charter, the Bank has limited resources and must make choices on where to invest our different capitals to ensure the future sustainability of the Bank. Therefore, the board has exercised its judgment and has chosen only the above audiences as the most significant to the Bank, as we are required to do by our regulator, for the next year and beyond.

In providing this forward-looking guidance,³⁶ the board has based its judgments on information provided by management through their extensive stakeholder engagement process, on the Bank's prior integrated/financial/sustainability report(s), and on the board's independent judgment, similar to the manner that the board's audit committee engages our financial auditors independently from management, albeit with management's input. The board will update this forward-looking Statement of Significant Audiences and Materiality in one year, or sooner, if it judges that such earlier forward-looking guidance is warranted.

On behalf of the Board of Directors,

//s//

Chairman

¹ Eccles, Robert G. & Youmans, Tim, “The Climate Custodians,” MIT Sloan Management Review – Big Ideas: Sustainability, February 2016, <http://sloanreview.mit.edu/article/the-climate-custodians/>.

² Eccles, Robert & Youmans, Timothy. “Materiality in Corporate Governance: The Statement of Significant Audiences and Materiality,” Harvard Business School Working Knowledge, 2015. This paper has been significantly updated in the forthcoming Journal of Applied Corporate Finance paper as discussed in notes 6 and 7.

³ “[Custody Services, Comptroller’s Handbook](#),” U.S. Department of the Treasury, Comptroller of the Currency, Administrator of National Banks, January 2002 [as updated May 17, 2012], p. 1.

⁴ From a combination of [Trefis](#) data and from our review the SEC 10-Q filings for Q1-Q3 2015, we estimate the Big Three global custody asset market share as \$28.1 trillion for State Street, \$28.5 trillion for BNY Mellon, and \$20 trillion for JPMorgan Chase 20 trillion. These three combined account for approximately 61% of the \$124.8 trillion global assets under custody market. We estimate the next biggest market share custody bank is Citigroup with \$14 trillion in custody assets.

⁵ Federal Reserve \$4.4 trillion, European Central Bank \$3 trillion, Bank of Japan \$3.1 trillion, and Peoples Bank of China \$5.1 trillion, in Yardeni, Edward & Quintana, Mali, “[Global Economic Briefing: Central Bank Balance Sheets](#),” Yardeni Research, Inc., June 2016.

⁶ Eccles, Robert & Youmans, Tim “Materiality in Corporate Governance: The Statement of Significant Audiences and Materiality,” Journal of Applied Corporate Finance, Vol. 28, No. 2, Spring 2016 (forthcoming). This paper is a significant update to the paper cited in note 1.

⁷ Since issuing our working paper (Eccles, Robert & Youmans, Timothy. “[Materiality in Corporate Governance: The Statement of Significant Audiences and Materiality](#),” Harvard Business School Working Knowledge, 2015), we have now expanded its underlying legal research to 34 countries, including all of the G20. This research is continually updated and is hosted in the [Duty of Board Directors](#) section of the at the American Bar Association Sustainable Development Task Force web site and in the [Sustainability & The Fiduciary Duty of Boards of Directors](#) section of the UN Global Compact web site.

⁸ Ibid.

⁹ “Custody Services, Comptroller’s Handbook.”

¹⁰ “[National Banks Active As of 12/31/2015](#),” U.S. Department of the Treasury, Comptroller of the Currency, Administrator of National Banks.

¹¹ “[Large Bank Supervision](#),” U.S. Department of the Treasury, Comptroller of the Currency, Administrator of National Banks, January 2010 [Updated 2012, 2013, 2014, 2015].

¹² According to the 10-K filings of each of the Big Three, their global custody banks are subsidiary corporations of bank holding companies, as such these banks have boards of directors. See note 14 for the OCC’s discussion of the relationship between the board of the subsidiary national bank and its parent holding company.

¹³ Eccles, Robert G. & Youmans, Tim, “[Why Boards Must Look Beyond Shareholders](#),” MIT Sloan Management Review, Big Ideas: Sustainability, September, 2015.

¹⁴ Padro, Miguel, “[UNREALIZED POTENTIAL: MISCONCEPTIONS ABOUT CORPORATE PURPOSE AND NEW OPPORTUNITIES FOR BUSINESS EDUCATION](#),” THE ASPEN INSTITUTE BUSINESS & SOCIETY PROGRAM, MAY 28, 2014, note 8, p.12

¹⁵ “[Duties and Responsibilities of Directors, Comptroller’s Handbook \(Section 501\)](#),” U.S. Department of the Treasury, Comptroller of the Currency, Administrator of National Banks, Narrative - March 1990, Procedures - January 1998, pp. 1 -2

¹⁶ “[The Director’s Book, The Role of a National Bank Director, Directors Toolkit](#),” Office of the Comptroller of the Currency, Washington, D.C., 2010 (2013 reprint), p. 1.

¹⁷ Ibid, p. 26.

¹⁸ Ibid, p. 73.

¹⁹ Ibid, pp. 26-27. Given the significant governance implications of the “MAINTAIN APPROPRIATE RELATIONSHIPS WITH THE PARENT HOLDING COMPANY AND BANK SUBSIDIARIES” section, we include the full section here:

A bank that is part of a holding company often has a different operating environment from an independent bank. A bank holding company can be a source of strength for its subsidiary banks and may

determine policies and perform key bank functions. The holding company's directors may oversee and review the role and responsibilities of a subsidiary bank's board of directors. A director who serves on the board of both a bank and its holding company must comply with the director's fiduciary duties to the bank, including the duty of loyalty. This duty bars conflicts of interest that may arise when actions that are in the best interest of the holding company conflict with those that are in the best interest of the bank.

For its part, the primary duty of the subsidiary bank's board of directors is to protect the bank. The bank's board must carefully review holding company policies that affect the bank to ensure that they adequately serve the bank. The board is responsible for either approving or recording its lack of approval of holding company directives that affect the bank and then monitoring those directives. If the board is concerned that the holding company is engaging in practices that either may harm the bank or are otherwise inappropriate, the board should notify the holding company and discuss modifications. If the holding company's board does not respond to the bank's concerns, the bank's board should dissent on the record and consider action to protect the bank. The bank's board should hire an independent legal counsel or accountant if it decides it is necessary. The board also may raise its concerns with bank supervisors.

A diversified bank holding company that has nonbank subsidiaries raises additional concerns that a bank board must consider. For example, the board of a holding company's subsidiary bank should be aware of the activities and condition of its holding company affiliates. No bank operates in a vacuum, and an affiliate's unsafe and unsound activities could adversely affect the bank's reputation as well as its condition. Certain transactions with affiliates may not be in the best interests of the bank and, in some cases, may be unlawful. These may include unearned or excessive management or servicing fees charged by the holding company or its affiliates, pressure for excessive dividends, or requests that the bank purchase low-quality assets from affiliates (which is specifically prohibited).

The operating environment of a bank with subsidiaries raises other issues. The board at the bank level must oversee the subsidiaries and verify that effective controls are maintained. Representation on the subsidiary's board is one way to be certain that the bank's board participates in policy making. The bank's board should confirm that it has authority to audit operations and review findings of the subsidiary's own internal or external auditors.

²⁰ See note 14.

²¹ See note 14.

²² See note 3.

²³ "Custody Services, Comptroller's Handbook," p. 9: "Board and Management Supervision - National bank directors are expected to perform general supervision over a bank's activities. Directors may assign the administration of custody activities to such officers, directors, employees, or committees as they may designate. However, directors retain the overall responsibility for supervision. Any workable system or organization of a custody operation may be acceptable as long as the directors are fully aware of and are fulfilling their responsibilities," and p.1 "Global Custody Services - A global custodian provides custody services for cross-border securities transactions. In addition to providing core custody services in a number of foreign markets, a global custodian typically provides services such as executing foreign exchange transactions and processing tax reclaims. A global custodian typically has a sub-custodian, or agent bank, in each local market to help provide custody services in the foreign country..."

²⁴ "Directors of a national bank are accountable not only to their shareholders and depositors but also to their regulators. Banks are regulated in part because Congress provides for federal insurance of deposits while also subjecting banks to regulatory oversight. This regulatory oversight is appropriate because of the risks inherent in the banking system, the safety net provided by deposit insurance, and the importance of a safe and sound banking system to the nation's economy," in "[The Director's Book, The Role of a National Bank Director, Directors Toolkit](#)," p. 1.

²⁵ "[Duties and Responsibilities of Directors, Comptroller's Handbook \(Section 501\)](#)," U.S. Department of the Treasury, Comptroller of the Currency, Administrator of National Banks, Narrative - March 1990, Procedures - January 1998, p. 5: Under the section titled "Directors' Responsibilities," the final enumerated responsibility is "To ensure that the bank has a beneficial influence on the economy of its community ... Directors, therefore, have a

continuing responsibility to the community to provide those banking services that will be conducive to well-balanced economic growth.”

²⁶ <http://www.clientearth.org/what-we-do/>

²⁷ [SASB Accounting Metric FN0103-18](#) lists the technical protocol. This metric is included in the [SASB standards for Asset Management & Custody Activities](#) under the “Integration of ESG Risk Factors into Investment Management and Advisory” topic. See [navigator.SASB.org / Home / Financials / Asset Management & Custody Activities](http://navigator.SASB.org/) at <https://navigator.sasb.org/financials/asset-management-and-custody-activities/fn0103-06/fn0103-06-04>.

²⁸ Eccles, Robert G. & Youmans, Tim, “The Climate Custodians.” MIT Sloan Management Review.

²⁹ [JPMorgan Chase & Co. “Corporate Governance Principles,”](#) Section 3.1.

³⁰ [BNY Mellon “Corporate Governance Guidelines,”](#) Section II-A.

³¹ [State Street “Corporate Governance Guidelines,”](#) February 2016, p.3.

³² [JPMorgan Chase & Co. “2015 10-K Annual Report” filing,](#) February 23, 2016, p. 111.

³³ State Street “Corporate Governance Guidelines.”

³⁴ Padro, Miguel, “UNREALIZED POTENTIAL: MISCONCEPTIONS ABOUT CORPORATE PURPOSE AND NEW OPPORTUNITIES FOR BUSINESS EDUCATION,” THE ASPEN INSTITUTE BUSINESS & SOCIETY PROGRAM, MAY 28, 2014, p. 8, citing in note 29 Strine, Leo Jr., “The Social Responsibility of Boards of Directors and Stockholders in Change of Control Transactions: Is there any “there” there?,” Southern California Law Review, Vol 75:1169, (Sept. 2002).

³⁵ Millstein, Ira. M, Gregory, Holly J., Altschuler, Ashely R. (Weil, Gotshal & Manges LLP), “Fiduciary Duties Under U.S. Law,” AMERICAN BAR ASSOCIATION International Developments Sub-Committee on Corporate Governance, pp. 34-38. <http://apps.americanbar.org/buslaw/newsletter/0026/materials/46.pdf>.

³⁶ Eccles, Robert & Youmans, Tim “Materiality in Corporate Governance: The Statement of Significant Audiences and Materiality,” Journal of Applied Corporate Finance, Vol. 28, No. 2, Spring 2016 (forthcoming)