

ROYAL DUTCH SHELL

Royal Dutch Shell (Shell) is a worldwide group of oil, gas and petrochemical companies that explores for, produces and trades in a range of energy resources. Royal Dutch Shell also has a broad portfolio of hydrogen, biofuels, wind and solar power interests, and also provides consultancy and technical services as well as research and development expertise to the energy industry. Royal Dutch Shell is active in more than 130 countries and territories, and employs 108,000 people worldwide.

Governance

Shell's *Business Principles* guide the company's operations:

- Economic
- Competition
- Business Integrity
- Political Activities
- Health, Safety, Security and the Environment
- Local Communities
- Communication and Engagement
- Compliance

They include a commitment to contribute to sustainable development and to respect human rights. The Shell Board of Directors is responsible for the Group's performance, and Board Committees assist in their respective governance responsibilities. The Social Responsibility Committee reviews the policies and conduct of Shell with respect to the *Business Principles* as well as the Group's health, safety and environment (HSE) policy and other relevant Group policies and standards. This committee is composed of non-executive directors.

The Chief Executive is responsible for sustainable development (SD). On his behalf, the Corporate Affairs Director chairs the Group Sustainable Development and Health, Safety and Environment (HSE) Executive. Its members are the executives responsible for social performance, HSE and security in each business and the company-wide head of these functions. The Committee reviews performance and sets priorities, key performance indicators and targets.

An SD/HSE Panel supports the SD/HSE Executive. It is composed of senior functional experts from each major Business and the corporate centre.

Country Chairs – the most senior Shell representative in a country or cluster of countries - are responsible for ensuring application of policies and codes of conduct in a country or group of countries. All Country Chairs must write an annual letter to the executive Board member responsible for their region on issues relating to the *Business Principles*. A Business Integrity Advisor reviews the letters of assurance and advises both the Country Chair and the Managing Director. Shell also has a Chief Ethics and Compliance Officer.

Shell's different businesses – Exploration and Production, Gas and Power, Oil Product and Chemicals, Renewables- have SD support. For example, SD is built into the portfolio of the Corporate Support Executive Vice President, Exploration and Production. Integrating SD into existing governance structures helps to better ensure SD considerations are factored into decision-making processes.

In 2005, the existing Executive Vice President, Renewables and Hydrogen, took on the additional role of Executive Vice President, CO₂. This position reports directly to the Executive Director, Gas and Power, who is also a Board member and is responsible for the delivery of the Group CO₂ strategy and supporting technologies. The CO₂ Group is responsible for the development and deployment of CO₂ mitigation technologies and the Group CO₂ strategy.

The Group measures its performance through a number of key performance indicators. The Group Scorecard highlights four key performance factors that together provide a summarized overview of the Group's performance – SD

accounts for 20% of the scorecard rating.

Business Processes

Strategic Planning: Shell uses global scenarios to cast light on the context in which the Group operates, to identify emerging challenges and to foster adaptability to change. These scenarios are used to help review and assess strategy. Sustainable development considerations are built into these scenarios. Shell-wide scenarios looking out 25 years are run every two-three years; in depth energy scenarios out to 2050 are done every five-six years.

As described by Shell using the metaphor of air navigation, the work of the Shell Scenarios team is designed to help charter routes across three interrelated levels:

- The Jet Stream level of long-term predetermined trends, uncertainties, and forces;
- The Weather Systems that reflect specific features of key regions as influenced by the Jet Stream context; and
- Market-level trends and turbulences.

With the help of the central scenarios team, individual businesses also create their own scenarios – at business and regional level - to inform and test their strategic plans.

Business Planning: Shell uses a business alignment tool to help individual operations measure their alignment with the *Business Principles*.

It also runs a Shell-wide issues management process, where environmental and social issues from the different businesses and regions are prioritised and managed. Input from this process is fed into the business planning process.

Business Development: Shell's *Business Principles* state that investment decisions must take into account social and environmental considerations and an appraisal of the security of the investment. This can be exemplified in the decision-making to move forward on a development project in the Gas and Power business unit. Projects must pass through a "funnel", and only projects that meet specific criteria at various stages of the funnel are executed. Projects at the early stage have to produce risk and issues matrices and engagement plans, which are considered integral tools to business development. There are also assurance checkpoints where an independent person assesses the project before it advances to the next phase. This process may include consideration of Shell's global risk matrix, but project teams are more likely to bring in experts to brainstorm specific risks and issues that they might face if this project goes ahead rather than apply the full global risk matrix. There are decision points in the business development process where specific reporting requirements ensure that the global HSE perspective is brought to bear on decisions.

For business development in the upstream business (Exploration and Production), there are significant steps and tools that integrate SD elements into decision-making, such as opportunity framing and SD workshops, impact assessment processes, country entry reports, and checklists that integrate SD considerations. These tools allow managers to frame options, identify issues, prepare a work plan, mitigate risks, and develop business opportunities.

The functional objective of Shell's Contracting and Procurement Division is to help the company achieve its SD objectives through the management of issues such as contractor safety and local content, which looks at whether Shell has an opportunity to add value in the local economies in which it is working. These issues are managed as an integrated part of doing business, which includes checkpoints in the contracting and procurement process, and the expectation that these issues would be explicitly addressed in contracting strategies.

The impact of CO₂ is a consideration for mergers and acquisitions as well as product development. The company looks at the impacts of mergers and acquisitions vis-à-vis alignment with the company's *Business Principles*. The impact of new products on CO₂ is also explored. The company's approach to CO₂ management is high on the agenda, and taken into account early in business development decisions.

Shell's *Business Principles* are promoted with joint venture partners, contractors and suppliers, and Shell has monitoring systems in place to ensure adherence and reporting on indicators such as the number of countries where Shell's *Business Principles* are included in contracts; the number of countries where contractors, sub-contractors and suppliers have been screened for compliance with *Business Principles*; and the number of contracts cancelled and joint ventures divested due to incompatibility with the *Principles*.

Risk Management: The Group takes a risk-based approach to internal control. Management in the Group is responsible for implementing, operating and monitoring the system of internal control, which is designed to provide reasonable assurance of achieving business objectives. Related requirements are set out in a Statement on Risk Management, which describes the methodology to be followed to manage risks to objectives. The control framework is supported by a set of risk-based standards that establish rules and instructions on enterprise-wide risks that require common treatment across the Group. Identified risk factors at the global level include sustainability issues such as impacts of climate change, doing business in politically sensitive or unstable areas, and loss of business reputation due to perceived failure to meet the *Business Principles*.

In addition to global risk management, all businesses must have a risk management system framework in place that takes local contexts into consideration. Each business has to maintain its own risk matrix that includes "incident" risk (e.g. operating in sensitive countries-security and human rights-plant explosion, commercial risk associated with project financing, resettlement, etc.) that are captured at local, regional, and/or global levels depending on their materiality and applicability to all of Shell's businesses.

Shell also uses the input of external expert panels to inform risks as these panels provide feedback to the company on issues of significance (e.g. animal testing).

Project Management: Shell's project management approach integrates the use of impact assessments and stakeholder management plans, and any new projects must have a stakeholder engagement plan in place. Once a project moves forward, the Group Diversity Framework requires annual diversity plans, and a human rights compliance tool provides managers with a step-by-step approach to help them avoid violating the basic human rights of employees and local communities during a project. Where necessary, Shell also employs a Resettlement Action Plan in accordance with World Bank standards.

CO₂ management is integrated into project management. All projects must include expected future costs of emitting CO₂ in their base economics, and decisions are taken on a CO₂-cost adjusted basis. At the project development level, there is a checklist and guidance on how to take account of CO₂ related issues. CO₂ costs are included in a project's base economics.

Efforts are also underway to develop tools that integrate biodiversity considerations into business practices.

Disclosure: Shell's Annual Report/20F filing includes a six-page section on "Environment and Society" that discusses the company's HSE standards and commitments,

climate change, safety, biodiversity, and being a good neighbour. It provides performance data on the company's key performance indicators in this area. Shell's Sustainability Report and Environment and Society website provide extensive and highlight transparent disclosures in this area.

Assurance: Shell has a variety of processes for obtaining assurance on the adequacy of risk management and internal control. These include:

- A structured process to identify and review risks to the achievement of Group objectives;
- A formalised self-appraisal and assurance letter process by which assurance is provided on compliance with Group standards;
- Risk-based audits of the Group's operations by Internal Audit;
- A business control incident reporting process; and
- An ethics and compliance program.

These established processes allow the Board, via the Audit Committee, to regularly consider the overall effectiveness of the system of internal control and to perform a full annual review of the system's effectiveness.

Every Shell project requires an assurance plan that provides for different levels of assurance on different items, specifically around early stage project development (e.g. impact assessment), and at specific "stage gates", including:

- Value assurance reviews – new projects are reviewed at regular intervals to assess their ability to succeed on many dimensions – technical, financial, and also environmental and social. For those projects that are high on the sustainable development risk/opportunity radar, ensure that an HSE/environmental, social, or external affairs representative is on the review team, or a combination of all three.
- Opportunity framing workshops – generate framework for opportunities to ensure that SD is taken into consideration. These workshops are held for every major opportunity. Shell is considering integrating an explicit and mandatory SD step in this process.

Shell uses external experts as a form of third-party assurance on the functionality and success of different projects and programs (e.g. community development projects, animal testing programs, etc.). Shell also uses an External Review Committee to provide assurance of its Sustainability Report (according to the AA1000 Assurance Standard). Shell has also used external assurance in certain geographic locations to test the accuracy and completeness of HSE and social investment data. Its Annual Report/20-F is assured by its external financial auditors.

Shell regularly audits its facilities' HSE management systems, and all major plants are required to be externally certified to international environmental standards (e.g. ISO 14001).

Independent management review boards review contracting strategies to ensure that they comply with corporate strategies.

Stakeholder Engagement

Community Relations:

The incorporation of the company's responsibilities to various stakeholders into its *Business Principles* (via the *Principles* regarding local communities, and communication and engagement) illustrates a strong level of commitment to stakeholders and integration of community relations into the business processes. Shell is committed to consulting with international and local stakeholder groups before making investment decisions, and has also committed to provide full and relevant information to legitimately interested parties on its activities.

It is a requirement that any new project have a stakeholder engagement plan

ROYAL DUTCH SHELL

in place, and Shell businesses produce a number of country or project-specific environmental and social performance reports to enhance local stakeholder engagement.

Stakeholder engagement is an integral part of the issues management process, and stakeholders are systematically identified and prioritized per issue. A central Social Performance Management Unit in the corporate centre provides expertise, challenge and support to projects and facilities in this area, and is composed of development experts, former NGO members, social workers etc. with professional experience/training in this area.

Investor Relations: Shell's aim is to integrate SD information as much as possible into regular investor briefings. The company also co-operates with the many groups that provide investors with information and analysis about the environmental and social performance of companies, including the producers of the Dow Jones Sustainability Indexes, FTSE4Good, Goldman Sachs Global Energy Environmental, Social and Governance Index, and the Carbon Disclosure Project.

Human Resources

Recruitment and Orientation: Shell's commitment to and performance on SD is an integral part of the company's branding and the way it presents itself to prospective employees. SD themes are an integral part of applicant assessment and new staff on-boarding processes.

Every two years, Shell surveys all employees on their feelings about Shell and their experiences at work. This helps the company to identify problems and assess staff morale. Detailed results of the 2006 survey have been communicated to staff and plans are being put in place to address the areas of weakness identified at local, business and company-wide levels.

Training: An SD mindset has been integrated into the main leadership development programs – the Group Business Leadership Program and Executive Leadership Program. It is also an integral part of the curriculum in Shell's Project Commercial Academies, set up in 2005 and 2006 respectively to raise the skill level of project managers and key commercial staff.

In addition, Shell is using an e-learning tool developed by the World Business Council for Sustainable Development and Cambridge University in the UK on the business case for SD, to help embed SD thinking into Shell's culture. The tool is made available on a voluntary basis, with the incentive of a certificate for everyone who completes the program. Shell also includes this e-learning in the "on-boarding kit" for all new employees.

Other training includes:

- Modules on SD in senior executive training and business management courses (including elements such as biodiversity, child labour, etc.);
- Leadership development courses;
- Relevant SD training provided to individual project teams;
- Online and face-to-face training for employees on the company's *Business Principles*, including preventing bribery and corruption;
- Training guide on Human Rights Dilemmas incorporated into *Business Principles* training; and

ROYAL DUTCH SHELL

- Compulsory awareness programs and online training on the company's Code of Conduct.

Shell is also developing training programs on implementing biodiversity action plans. Sustainable development issues are integrated into the courses that are run jointly with leading business schools in Asia, Europe and the USA.

Shell also has in place an informal climate change network that spans all businesses and conducts webcasts, publishes a newsletter, runs web discussion forums, and is putting in place tools like internal discussion networks for sharing knowledge and best practice in this area.

Performance Appraisal and Compensation:

Shell uses its scorecard to appraise business performance and reward executives (of which 20% is based on sustainability). The scorecard includes key performance indicators to manage the company's operations, including environmental and social indicators. For nearly all Shell staff, this scorecard directly affects the level of annual bonuses. Employees are rewarded for personal performance and team achievements in contribution to sustainability, and senior staff rewards are also linked to their sustainability contribution.
