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Data privacy in the Information and Communication Technology sector

In an increasingly digitalized world, telecommunication services and IT companies are evermore associated with the collection of customer data and subsequent data privacy breaches. As a result, companies in the information and communication technology sector (ICT) sector are exposed to reputational, legal, and operational risks. At the same time, a proactive approach to managing privacy issues, by raising awareness or implementing different levels of privacy in products, for instance, can also result in opportunities. Therefore, investors should consider how companies manage privacy issues in their investments and engage with companies to help them understand best practices. Consequently, we believe that a roundtable with companies serves as an ideal engagement platform and allowing us to better understand issues surrounding data privacy from a company's perspective.

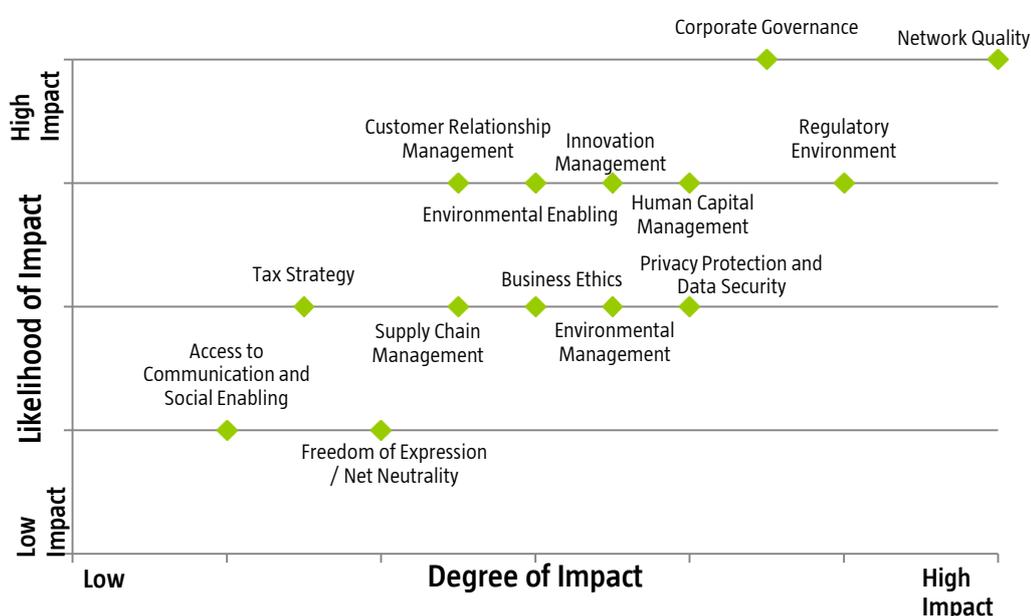
Relevance for investors

The issue of data privacy poses risks to companies from a broad range of industries due to the importance of technology and digital access across sectors. The information and communication technology sector (ICT) sector is particularly exposed to risks associated with privacy breaches since business models of these companies are fully built around electronic data. The types of financial impacts are manifold and include cost impacts through fines from law suits or revenue impacts due to reputational damage, boycotts of products & services or general loss of contracts due to mistrust.

Discredit by the financial market can also result in divestiture and consequently lower share prices. Therefore, we see a relatively high degree of financial impact from privacy issues for ICT companies (as shown in the horizontal axis in the materiality matrix in figure 1). But as there is uncertainty of how companies are affected, the likelihood of a financial impact is only medium (see vertical axis in the materiality matrix in figure 1). Reasons why the financial impact might not directly materialize are for example a lack of options for customers/users to switch to other products, other service providers facing the same issues or customers/users simply not fully understanding privacy implications.

As elaborated above, privacy issues are financially relevant but the timing and the level of impact are not easy to assess financially. Therefore, we believe that talking to companies can provide us with valuable insights into how to analyze companies' efforts in dealing with customer/user privacy.

Figure 1: Materiality matrix for the telecommunication services sector



Source: RobecoSAM

Engagement objectives

In early 2015, we started an engagement program on data privacy. We have conducted extensive research into the topic and have selected companies for an in-depth three year engagement focused on improving their policy, risk management, transparency and collaboration with regard to data privacy. With RobecoSAM’s fully integrated engagement and investment approach, we aim to increase the added value of our engagement by focusing on financially material issues directly linked to company profitability that are directly relevant for investors.

For our dialogue with the ICT companies, we defined the following four objectives:

Policy objective

Companies should implement comprehensive human rights policies that relate specifically to risks relevant for data privacy and freedom of expression. The policy should apply to the company and, where appropriate, its supply chain. The policy should also identify a number of targets that lead to the effective prevention of (future) breaches and the policy should be effectively implemented.

Risk management objective

Companies should assess human rights risks related to data privacy and freedom of expression and have a strategy of communicating the results of these risk assessments. Risk assessments should be an on-going process at the start of a new activity, a new business relationship, major change in business or changes in the operating environment. Afterwards, measures to mitigate the identified risks should be implemented. Those measures could for example include training of employees working closely with sensitive customers’ data.

Transparency objective

Under this objective, we will monitor companies’ efforts to improve transparency and disclosure in relation to the assessment and management of risks related to data privacy and freedom of expression. Where companies have been the subject of allegations relating to data privacy and/or freedom of expression, we will seek evidence of a response to these allegations and determine whether remedial measures have been implemented.

Partnerships and collaboration objective

We expect companies to collaborate and build partnerships with key players from across the ICT sector, including peers, vendors, business partners, customers, NGOs and government organizations to work together to manage human rights risks relevant to data privacy and freedom of expression.

The roundtable

As part of our engagement program and with the aim of further building our expertise on the topic, we invited companies to a roundtable discussion to exchange ideas and share experiences related to the topic of data privacy. All of the invited companies participated in the RobecoSAM Corporate Sustainability Assessment (CSA). The roundtable to discuss data privacy in the ICT sector was held in Horgen, Switzerland, immediately before the RobecoSAM Forum at the end of September. Seven ICT companies from Europe, the US and Asia met with Robeco and RobecoSAM analysts and engagement specialists.

Participants discussed questions such as: 'How material is the issue of data privacy for ICT companies?', 'How do companies assess and quantify the risk?' and 'What type of risk mitigation measures can be put in place to keep customers' trust?' We also touched on the opportunities arising from the topic.

Roundtable takeaways

The key takeaways from the roundtable were:

1. RAISING CUSTOMER AWARENESS

Companies consider raising awareness to be important. Customers are generally unaware of what happens with their data and companies feel an obligation to be proactive and make sure the customer is making the right decision. This includes educating consumers about their own responsibilities related to data protection, but also includes providing them with a more accessible privacy statement so that customers can actually see what they agree to. Difficulties may arise from differences in the notice of personal privacy, which differs per country but also between different age groups. Companies mentioned examples in which customers thought that the company's products were interfering with their privacy rights but the product was actually not. Therefore, raising awareness of how customers' information is handled should help to better match customers' expectations of data privacy with the level of data privacy inherent to a specific product.

2. THE IMPORTANCE OF COLLABORATION

Partnerships and collaborations with other industry players are key. Companies discuss latest developments, share knowledge and work together in the sector to manage privacy risks. A company's level of participation in these stakeholder groups can be an indication of the level importance it assigns to the topic. Industry collaboration was also mentioned as very important by companies in our engagement program. Especially when it comes to government requests to provide customer/user information, collaboration, as for example done through the 'Telecommunications Industry Dialogue', is helpful to find a structured industry wide approach to handling such requests.

3. PRIVACY BY DESIGN

For many ICT products, privacy considerations should be taken into account early in the product development process. A systematic approach ensures that privacy is taken into account in the relevant process steps and helps to create accountability. During the roundtable, one company from the IT hardware sector mentioned that it can become very costly if changes have to be made to products late in the development process in case privacy features were not thoroughly implemented in earlier stages. It was also mentioned that privacy by design offers an opportunity for companies to provide products that feature different levels of privacy.

4. TECHNOLOGY MOVES FASTER THAN REGULATION

Companies feel that they need to be proactive in their approach as regulation has kept up with technological developments. But it is crucial for companies not to rush and risk that there are legal issues in the future. As an example the rush to 'big data' was mentioned. It was explained that companies first have to sit down with customers to define customer goals and expectations in order to define the right level of privacy. If not done properly, the company risks having disputes with clients in the future. Regulations also differ per country or region. Therefore companies need to set their own corporate standard in order to work in a consistent manner across jurisdictions.

5. SECURITY AND PRIVACY GO HAND IN HAND

The companies agreed that without security there is no privacy. In other words, companies can do their utmost to handle data conscientiously but still fail if data is stolen or lost. Therefore, it is crucial to view privacy issues as closely linked to data security. However, from a technology view point, data security is much more complex and requires in depth expertise. It was therefore decided not to dive deeper into this topic at the roundtable.

6. NOT ONLY A RISK, BUT ALSO AN OPPORTUNITY

At the end of the roundtable, we explored opportunities relating to data privacy. The companies stressed that beyond risk management, concerns over data privacy offer an opportunity to differentiate products based on different levels of privacy. But in order to be successful, the needs of customers/users must be well understood. Exploiting data must be done very carefully because data belongs to the customer. One participating company explained that different customers view privacy and data protection differently. Younger people for example are willing to share more personal information if they can get a benefit in terms of a better service. Consequently, offering customers choices for sharing their data offers new product opportunities. As mentioned in the first takeaway from the roundtable, it is very important that customers are aware of how their data is being used and that they can see how they benefit from sharing data. Finally, in order to receive explicit or implicit consent from customers/users to use their personal data for additional services or advertising, trust remains key.

7. INVESTOR FOCUS

The companies generally felt that investors should focus less on the risk side of privacy but rather look at the opportunities from applying the right level of data privacy to specific products. It is important for investors to understand to what extent companies are looking at opportunities, what guidance they use and how their governance around it is organized. Ultimately, corporate culture is very important to managing privacy issues successfully because there is usually not a clear definition on what is acceptable and when privacy rights are breached. It also needs a clear understanding of customers' needs and expectations.

Conclusion: delivering value to companies and investors

The participating companies considered the roundtable to be a success because they were able to speak freely with their peers, share experiences and hear the investor's viewpoint. Our dialogue with companies creates value for companies as we clarify shareholders' expectations and help to strengthen the link between sustainability initiatives and financial performance. This way, companies can increase their competitiveness and attract investors with longer-term investment horizons.

The roundtable also provided us with unique insights into how companies understand privacy risks and opportunities. We were pleased to see how advanced the participating companies are in managing the complex issue of data privacy. Investors generally still perceive data privacy predominantly as a risk and thus overlook the opportunities. Because privacy needs and expectations differ among people and organizations, a company must understand those needs and expectations. At the same time, it has to ensure that all stakeholders are aware of what a company does and doesn't do with their data. Raising awareness, therefore, is critical to managing privacy. If there is a clear understanding of how data is handled, products with different privacy levels can be designed and offered. And by doing so, companies can differentiate their products from competitors.

As an investor focusing exclusively on Sustainability Investing, RobecoSAM will continue to monitor the ICT industry's progress on data privacy. Based on the main conclusions from the roundtable, we strive to better reflect how companies interact with stakeholders in relation to privacy and how opportunities are captured by companies, both in the DJSI assessment and in our investment cases. We will continue to engage with individual companies and hold similar roundtables in the future, as it has proven to be a valuable engagement tool that has contributed to our understanding of issues that are relevant to corporate profitability.



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About RobecoSAM

Founded in 1995, RobecoSAM is an investment specialist focused exclusively on Sustainability Investing. It offers asset management, indices, engagement, voting, impact analysis, sustainability assessments, and benchmarking services. Asset management capabilities cater to institutional asset owners and financial intermediaries and cover a range of ESG-integrated investments (in public and private equity), featuring a strong track record in resource efficiency theme strategies. Together with S&P Dow Jones Indices, RobecoSAM publishes the globally recognized Dow Jones Sustainability Indices (DJSI). Based on its Corporate Sustainability Assessment, an annual ESG analysis of 2,900 listed companies, RobecoSAM has compiled one of the world's most comprehensive databases of financially material sustainability information.

RobecoSAM is a member of the global pure-play asset manager Robeco, which was established in 1929 and is the center of expertise for asset management within the ORIX Corporation. As a reflection of its own commitment to advocating sustainable investment practices, RobecoSAM is a signatory of the UNPRI and a member of Eurosif, ASrIA and Ceres. Approximately 130 professionals work for RobecoSAM, which is headquartered in Zurich. As of June 30, 2014, RobecoSAM had assets under management, advice and/or license in listed and private equity* of approximately USD 10.7 billion. Additionally, RobecoSAM's Governance & Active Ownership team** had USD 85.1 billion of assets under engagement and USD 53 billion of assets under voting.

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