

## Firms Face Increased Reputational Risk for Corporate Responsibility Failures

### Executive Summary

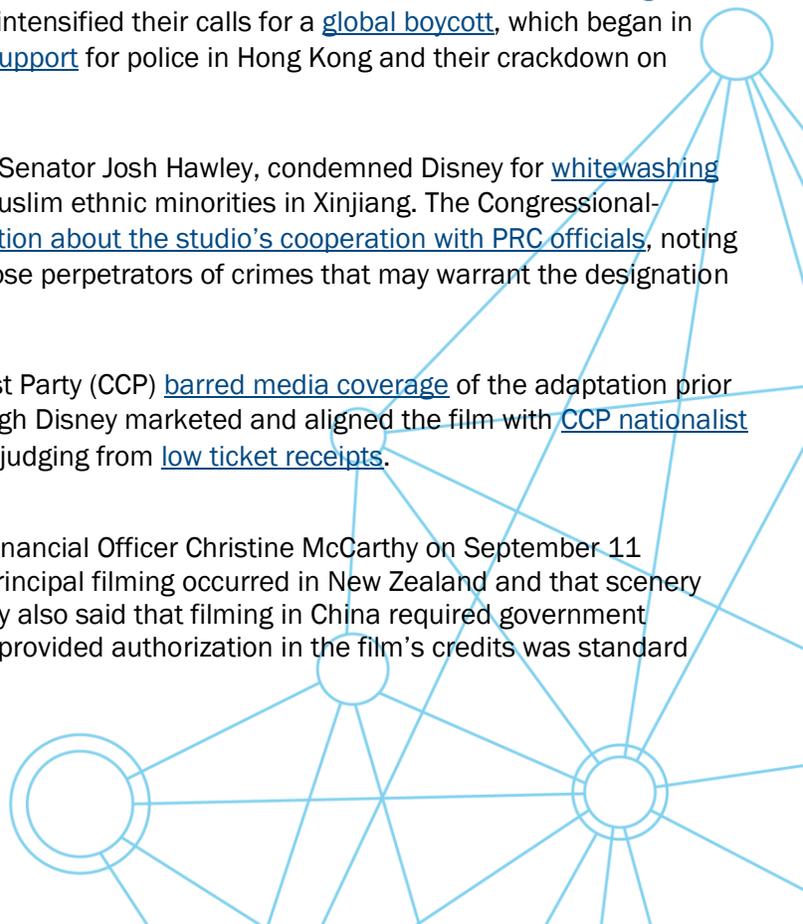
Recently, Walt Disney Studios and metals and mining corporation Rio Tinto found themselves embroiled in scandals stemming from significant environmental, social, and corporate governance (ESG) failures, highlighting the need for firms to conduct research into potential reputational risks—in addition to due diligence and compliance checks—before engaging in business activities. Disney’s use of shooting locations in the Xinjiang Uyghur Autonomous Region (XUAR) in 2018 for the movie *Mulan* and Rio Tinto’s [demolition of](#) 46,000 year old Aboriginal caves in the Juukan Gorge on May 24, 2020 resulted in significant backlash and reputational damage for the two multinational firms.

### Disney

Disney’s release of the live-action adaptation of its animated hit *Mulan* in September 2020 quickly became controversial after one of its shooting locations was [identified](#) as XUAR—the western province in the People’s Republic of China (PRC) where approximately [2,000,000](#) Uyghur and Turkic Muslim ethnic minorities are detained in reeducation camps by the Chinese government and used as slave labor. Disney also thanked eight state entities in the film’s closing credits, including Turpan’s Public Security Bureau, which was named to the Commerce Department’s BIS Entity List in [October 2019](#) for its [primary role](#) in administering China’s internment system.

- Global media outlets, including [Hollywood Reporter](#), [The New York Times](#), [BBC](#), [The Guardian](#), [Bloomberg](#), and [Al Jazeera](#), reported on the controversy, and activists intensified their calls for a [global boycott](#), which began in August 2019 after the film’s star, Liu Yifei, [voiced support](#) for police in Hong Kong and their crackdown on protestors.
- Prominent legislators in the United States, such as Senator Josh Hawley, condemned Disney for [whitewashing](#) the ongoing atrocities against Uyghurs and other Muslim ethnic minorities in Xinjiang. The Congressional-Executive Commission on China [requested information about the studio’s cooperation with PRC officials](#), noting the company’s choice, “offers tacit legitimacy to those perpetrators of crimes that may warrant the designation of genocide.”
- In response to the backlash the Chinese Communist Party (CCP) [barred media coverage](#) of the adaptation prior to its release in China on September 11. Even though Disney marketed and aligned the film with [CCP nationalist narratives](#), local interest in the film appears muted judging from [low ticket receipts](#).

In Disney’s first public response to the controversy, Chief Financial Officer Christine McCarthy on September 11 [downplayed](#) the company’s ties to Xinjiang by noting that principal filming occurred in New Zealand and that scenery was filmed across 20 separate locations in China. McCarthy also said that filming in China required government authorization and acknowledging government entities that provided authorization in the film’s credits was standard



practice. However, McCarthy also noted that the controversy, “[generated a lot of issues](#)” for Disney, although she failed to provide details or explain why Disney chose to film in the region in August 2018, when the media was [reporting](#) on China’s policies toward the Uyghurs and the United States first considered [sanctioning](#) responsible officials.

## Rio Tinto

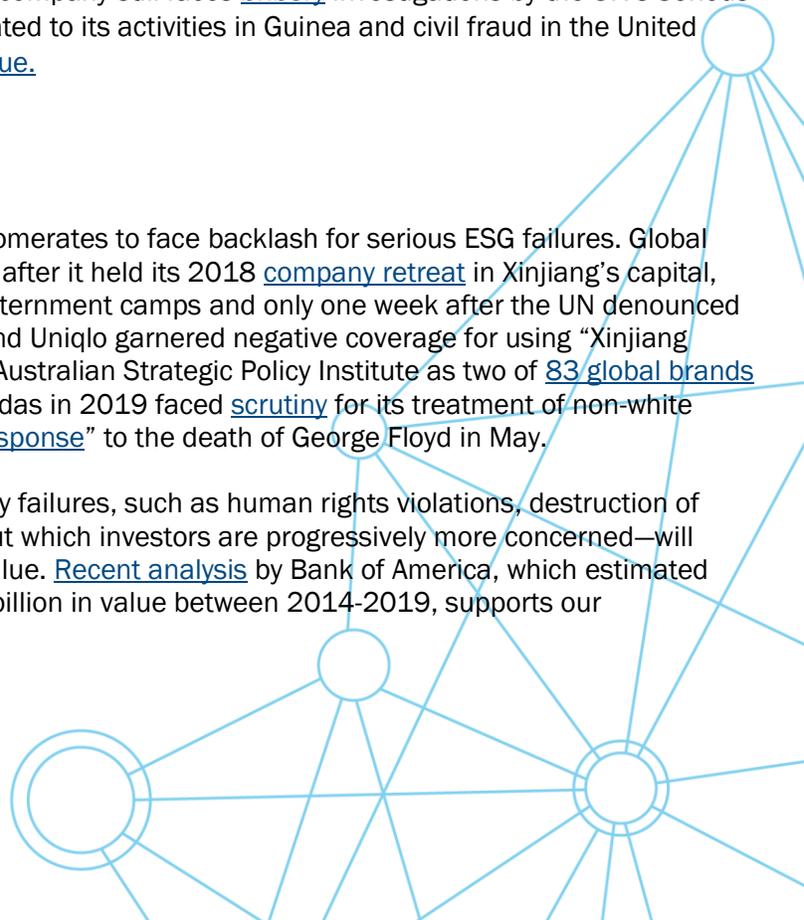
In May 2020, backlash against Rio Tinto led the company to admit that its demolition of Aboriginal caves in Australia was an, “[incomprehensible mistake](#),” especially because it knew of the site’s historical and cultural significance since at least [2014](#). After noting that the destruction took place during [National Reconciliation Week](#)—a state-sponsored program intended to heal relationships between Indigenous and non-Indigenous Australians—pressure from activists investors, politicians, and environmental groups led to the [resignations](#) of the company’s CEO, Chief Executive for Iron Ore, and Group Executive for Corporate Relations in September. Rio Tinto’s shareholders [expressed](#) serious concerns about executive accountability, highlighting the need for a comprehensive approach to ensure the best timing, messaging, and engagement with stakeholders of major projects.

- In August 2020, Rio Tinto published an [internal report](#) acknowledging that the company failed to meet its own standards to protect cultural heritage and work effectively with Indigenous groups. The company revoked performance-based bonuses for the three executives, and non-executive directors promised to donate 10 percent of their fees to the Clontarf Foundation, which supports Aboriginal education and employment.
- Rio Tinto has [faced previous scrutiny](#) for its corporate practices, including [labor disputes](#), [environmental degradation](#), and [human rights violations](#) around the world. Although COVID-19 is likely to [delay](#) federal inquiries into the demolition of Juukan Gorge, the company still faces [bribery](#) investigations by the UK’s Serious Fraud Office and the Australian Federal Police related to its activities in Guinea and civil fraud in the United States related to a [failed investment in Mozambique](#).

## Analysis

Disney and Rio Tinto are only the latest international conglomerates to face backlash for serious ESG failures. Global consulting giant, McKinsey, faced a public relations uproar after it held its 2018 [company retreat](#) in Xinjiang’s capital, Kashgar, roughly four miles from one of the city’s largest internment camps and only one week after the UN denounced China’s mass detentions. Japanese clothing brands Muji and Uniqlo garnered negative coverage for using “Xinjiang Cotton” as a [selling point](#) in 2019 and were named by the Australian Strategic Policy Institute as two of [83 global brands](#) that benefit from Xinjiang forced labor. Sportswear firm Adidas in 2019 faced [scrutiny](#) for its treatment of non-white employees, and more recently was accused of a “[muted response](#)” to the death of George Floyd in May.

FiveBy assesses that firms linked to corporate responsibility failures, such as human rights violations, destruction of indigenous heritage, and racial discrimination—issues about which investors are progressively more concerned—will increasingly struggle to protect their public standing and value. [Recent analysis](#) by Bank of America, which estimated that failures to address ESG issues cost companies \$534 billion in value between 2014-2019, supports our assessment.



FiveBy also expects companies that fail to address ESG issues to face greater public and regulatory scrutiny. Legislators around the world are under pressure from voters to hold major [corporations accountable](#) for ESG breakdowns. The EU is showing increased support for the adoption of a [human rights-centered Magnitsky-style sanctions regime](#), similar to those enacted in the United States, Canada, and the UK. The Australian government is also reexamining its policies after [authorizing Rio Tinto in 2013](#) to demolish the Juukan Gorge under the Aboriginal Heritage Act of 1972.

FiveBy encourages corporate responsibility leads to closely follow the public and regulatory blowback associated with engagements with companies in Xinjiang. On September 14, Customs and Border Patrol issued [five withhold release orders](#) on products the administration assesses are produced by slave labor in XUAR, directing officers at all ports to withhold release on goods such as hair products, clothing, and computer parts, and signaling that companies could face considerable scrutiny and possible complications to their business relationships in the region. Firms that continue engaging with companies in Xinjiang are also at risk of violating US and international sanctions. In July 2020, the US government [issued an advisory](#), describing the risks and considerations for US firms with supply-chain exposure to entities engaged in human rights violations in XUAR.

