The Evolution of SEC Disclosure –

The Materiality of ESG Information and its Use by Investors

Sustainability Accounting Standards Board & Workiva

March 14, 2017
Obtaining Your CPE Credit

- One hour of CPE credit
- Four attendance questions asked during webinar
- Logged in with correct contact information
Your Panelists

Janine Guillot
Director of Capital Markets Policy and Outreach, SASB

Robert Herz
Former Chairman, FASB.
Board Member of SASB, Workiva, Fannie Mae, Morgan Stanley

Rakhi Kumar
Head of ESG Investments and Asset Stewardship, State Street Global Advisors

Malcolm Ryerse
Director, Responsible Investment, Columbia Threadneedle Investments
Agenda For Today’s Webinar

• The SASB Perspective (8 minutes)
• The Corporate Reporting and Regulatory Landscape (8 minutes)
• The Investor Perspective (15 minutes)
• Panel Discussion and Q&A (30 minutes)

Learning Objectives:

• Gain a broader understanding of why investors care about ESG info and how investors use the information.
• Learn about the current regulatory environment as it relates to corporate reporting on sustainability issues.
• Understand the landscape and state of disclosure for climate-related risks.
Polling Question #1

What is your role?
Investors Care about Sustainability
A rapidly increasing share of global assets are managed with ESG issues in mind

**Trends in U.S. Sustainable, Responsible, & Impact Investing**
2005-2016

Today, **1 out of every 5 dollars** under professional management in U.S. managed under sustainable and responsible investment strategies.

![Bar chart showing trends in U.S. sustainable, responsible, & impact investing from 2005 to 2016](image)

**Key sustainability-related investor initiatives and Assets Under Management:**

<table>
<thead>
<tr>
<th>Initiative</th>
<th>AUM (US $)</th>
</tr>
</thead>
<tbody>
<tr>
<td>PRI</td>
<td>$59 trillion</td>
</tr>
<tr>
<td>CDP</td>
<td>$95 trillion</td>
</tr>
<tr>
<td>International Corporate Governance Network</td>
<td>$26 trillion</td>
</tr>
<tr>
<td>Investor Network on Climate Risk</td>
<td>$15 trillion</td>
</tr>
</tbody>
</table>

*Adapted from US SIF Foundation*
The SASB Difference
SASB standards are created for the market, by the market

MATERIAL
DECISION-USEFUL
COST-EFFECTIVE
INDUSTRY-SPECIFIC
EVIDENCE-BASED
MARKET-INFORMED
Evaluation of the Materiality of Sustainability Issues in Each Industry

SASB’s research and prioritization starts with a broad set of sustainability issues

Environment
- GHG emissions
- Air quality
- Energy management
- Fuel management
- Water and wastewater management
- Waste and hazardous materials management
- Biodiversity impacts

Social capital
- Human rights and community relations
- Access and affordability
- Customer welfare
- Data security and customer privacy
- Fair disclosure and labeling
- Fair marketing and advertising

Human capital
- Labor relations
- Fair labor practices
- Diversity and inclusion
- Employee health, safety, and wellbeing
- Compensation and benefits
- Recruitment, development, and retention

Business model and innovation
- Lifecycle impacts of products and services
- Environmental and social impacts on assets and operations
- Product packaging
- Product quality and safety

Leadership and governance
- Systemic risk management
- Accident and safety management
- Business ethics and transparency of payments
- Competitive behavior
- Regulatory capture and political influence
- Materials sourcing
- Supply chain management
Rigorous Process Drives SASB Standards
Standards for each industry are rooted in evidence and shaped by market input

Industry Research
Evidence of Financial Impacts

Industry Working Groups
2800 Market Participants

Evidence Vetting
Standards Council
Sub-Committee on Metrics Quality

Public Comment
90 days

Final Revisions

Provisional Standard
Average of 5 topics and 13 metrics

Standards maintenance
Ongoing
Robust Standards Designed to Provide Decision-Useful Information

SASB standards contain industry-specific disclosure topics, metrics, and guidance.

Industry-specific disclosure topics

Technical protocol for compiling data; activity metrics for normalization

Accounting metrics for each disclosure topic

Table 1. Material Sustainability Topics & Accounting Metrics

<table>
<thead>
<tr>
<th>TOPIC</th>
<th>ACCOUNTING METRIC</th>
</tr>
</thead>
<tbody>
<tr>
<td>Greenhouse Gas Emissions</td>
<td>Gross global Scope 1 emissions; percentage covered under a regulatory program, percentage by hydrocarbon resource</td>
</tr>
<tr>
<td></td>
<td>Amount of gross global Scope 1 emissions from: (1) combustion, (2) flared hydrocarbons, (3) process emissions, (4) directly vented releases, and (5) fugitive emissions/leaks</td>
</tr>
<tr>
<td></td>
<td>Description of long-term and short-term strategy or plan to manage Scope 1 emissions, emissions reduction targets, and an analysis of performance against those targets</td>
</tr>
<tr>
<td>Air Quality</td>
<td>Air emissions for the following pollutants: NOx (excluding NOx), SO2, volatile organic compounds (VOCs), and particulate matter (PM)</td>
</tr>
<tr>
<td>Water Management</td>
<td>Total fresh water withdrawn, percentage recycled, percentage in regions with High or Extremely High Baseline Water Stress</td>
</tr>
<tr>
<td></td>
<td>Volume of produced water and flowback generated; percentage (1) discharged, (2) injected, (3) recycled; hydrocarbon content in discharged water</td>
</tr>
</tbody>
</table>

Reserves Valuation & Capital Expenditures

Description

Estimates suggest that E&P companies are unlikely to be able to extract a significant proportion of their known, probable oil and gas reserves if GHG emissions are to be controlled to limit global temperature increases to greater risks. Regulatory limits on GHG emissions, together with improved competitiveness and energy technologies, could lower or reduce the growth in global demand, and therefore in gas products. Extraction costs could increase with regulations that put a price on GHG emissions, which could affect the net present value of oil and gas reserves. Regulatory actions that are more stringent or those focusing on industries with high emissions, could impair asset values substantially in the near term. Stewardship of capital resources and production decisions that take into account new requirements related to climate change mitigation actions can help prevent current asset impairment and enhance and creditworthiness.

Accounting Metrics

NR0101-22. Sensitivity of hydrocarbon reserve levels to future price projection scenarios

.122 The registrant shall conduct an analysis of its reserves to determine how several factors will affect its determination of whether the reserves are proved or probable.
SASB Materiality Map

A first view of exposure to material sustainability risks across a diversified portfolio

SASB Materiality Map™
SASB’s Materiality Map identifies likely material sustainability issues on an industry-by-industry basis. Click on a highlighted cell at the sector-level and then on any highlighted cell at the industry-level to see suggested accounting metrics and additional information for each issue.

<table>
<thead>
<tr>
<th>ISSUES</th>
<th>Health Care</th>
<th>Financials</th>
<th>Technology and Communications</th>
<th>Non-Renewable Resources</th>
<th>Transportation</th>
<th>Services</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Click to expand</td>
<td>Click to expand</td>
<td>Click to expand</td>
<td>Click to expand</td>
<td>Click to expand</td>
<td>Click to expand</td>
</tr>
<tr>
<td>Environment</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>GHG emissions</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Air quality</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Energy management</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Fuel management</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Water and wastewater management</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Waste and hazardous materials management</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Biodiversity impacts</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Social Capital</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Human rights and community relations</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Access and affordability</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Customer welfare</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Data security and customer privacy</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Fair disclosure and labeling</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Fair marketing and advertising</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Human Capital</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Labor relations</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Fair labor practices</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Employee health, safety and wellbeing</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Diversity and inclusion</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Compensation and benefits</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Complementary Efforts
Mandatory and voluntary reporting serve different purposes for different audiences

**Relevant Information**
All environmental, social, and governance topics of interest

**Material Information**
Sustainability factors *likely to affect the financial condition or operating performance of a company*

**Alignment is key**
(e.g., consistent approach to determining and disclosing “material” information, presentation of results)

**All Stakeholders**

**Investors**

© SASB
Polling Question #2

How would you characterize your sustainability disclosures?
The Corporate Reporting and Regulatory Landscape
The Pain Point for Investors
Investors lack tools needed to integrate sustainability into investment decisions

Investor Needs
Investor confidence in the quality of the ESG information received from issuers

29%

Issuer Reporting
Issuer confidence in the quality of the ESG information reported

100%


High degree of investor dissatisfaction with the current state of ESG disclosure

<table>
<thead>
<tr>
<th>Percentage of Investors Dissatisfied</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>82%</td>
<td>How risks and opportunities are identified and quantified in financial terms</td>
</tr>
<tr>
<td>79%</td>
<td>Comparability of sustainability reporting between companies in the same industry</td>
</tr>
<tr>
<td>74%</td>
<td>Relevance and implications of sustainability risks/issues</td>
</tr>
<tr>
<td>68%</td>
<td>Key performance indicators related to each identified material issue</td>
</tr>
<tr>
<td>57%</td>
<td>Process used to identify material sustainability issues</td>
</tr>
</tbody>
</table>

Source: PwC, Sustainability Goes Mainstream, May 2014
Reporting Burden for Companies
Multiple ESG questionnaires consume corporate resources and provide little value

A market standard could reduce the burden and risk of selective disclosure.

- Large-cap companies receive hundreds of information requests each year, leading to “questionnaire fatigue” and information asymmetry.
- On a 2016 Institute of Management Accountant (IMA) webinar survey of 100 members, 7.5% of respondents reported completing more than 250 ESG surveys per year.
- At GE, responding to over 650 ESG questionnaires involved more than 75 people at GE and took several months, “with virtually no value to (GE’s) customers or shareholders and even less impact on the environment.”

Designed for Integration into Mandatory Public Filings
An integrated reporting environment without regulation

US GAAP governs presentation of the financials

True and fair representation of performance on material factors

SASB Disclosure Topics and Metrics designed for integration into MD&A, risk factors, and other sections as appropriate
Definition of Materiality from an Investor’s Perspective
SASB is guided by U.S. securities law in identifying disclosure topics

US Supreme Court Definition

“Material information” is defined by the U.S. Supreme Court as presenting a substantial likelihood that the disclosure of the omitted fact would have been viewed by the reasonable investor as having significantly altered the “total mix” of information made available.


MD&A Disclosure Rules

- Item 303 of Reg SK requires disclosure of certain known trends and uncertainties
- Companies must evaluate:
  1. Likelihood of occurrence
  2. Effect on a company’s financial condition or results of operations
Current State of Disclosure
Opportunity to transform disclosure from boilerplate to metrics-based

STATE OF DISCLOSURE IN SEC FILINGS

Tools for Investors
Disclosure Intelligence tool in the SASB Navigator provides insight into disclosure

Disclosure Intelligence (beta)

4,300+ public filings

- Analyze disclosure quality
- Benchmark disclosure against industry peers
- Access disclosures on SASB topics

Demo available at navigator.sasb.org
Polling Question #3

Do your investors ask you about the impact of environmental, social and governance factors on your business?
The SASB Investor Advisory Group (IAG) comprises leading asset owners and asset managers who recognize the need for consistent, comparable and reliable disclosure of material, decision-useful ESG information.

IAG members:

- Encourage companies to disclose material and decision-useful ESG information to investors
- Believe standards would improve the quality and comparability of sustainability-related information
- Believe SASB’s approach—which is industry-specific and materiality-focused—will help provide investors with relevant and decision-useful information
- Agree to participate in SASB’s ongoing standards development process, so that outcomes best reflect investor needs
- Agree to encourage companies to participate in SASB’s ongoing standards development process, so that outcomes reflect both issuer and investor viewpoints
- Believe that SASB standards can inform integration of sustainability factors into investment and/or stewardship processes, such as corporate engagement and proxy voting
Rakhi Kumar
Head of ESG Investments and Asset Stewardship, State Street Global Advisors

Figure 1: SSGA's Framework for Evaluating a Company's Approach to Sustainability

**STEP 1**
Has the company identified material environmental and social sustainability issues relevant to the business?

**STEP 2**
Has the company assessed and, where necessary, incorporated those issues into their long-term strategy?

**STEP 3**
Has the company communicated its approach to sustainability issues and the influence of these factors on strategy?

Figure 2: Addressing Sustainability Issues: Questions for Boards

1. Has the company identified the sustainability issues material to the business?

2. Has the company analyzed and incorporated sustainability issues, where relevant, into its long-term strategy?

3. Does the company consider long-term sustainability trends in capital allocation decisions?

4. Is the board equipped to adequately evaluate and oversee the sustainability aspects of the company's long-term strategy?

5. Does the company's reporting clearly articulate the influence of sustainability issues on strategy?

6. Is the board incorporating key sustainability drivers into performance evaluation and compensation programs?
Malcolm Ryerse
Director, Responsible Investment, Columbia Threadneedle Investments

ESG Ratings Dashboard: Portfolios versus Benchmarks

Chart 1: ESG Rating Distribution for Portfolios vs. Benchmark

<table>
<thead>
<tr>
<th>Fund A</th>
<th>Benchmark</th>
<th>ESG Score Distribution</th>
</tr>
</thead>
<tbody>
<tr>
<td>AAA</td>
<td>3%</td>
<td>0%</td>
</tr>
<tr>
<td>AA</td>
<td>42%</td>
<td>0%</td>
</tr>
<tr>
<td>A</td>
<td>209%</td>
<td>0%</td>
</tr>
<tr>
<td>BBB</td>
<td>396%</td>
<td>0%</td>
</tr>
<tr>
<td>BB</td>
<td>27%</td>
<td>0%</td>
</tr>
<tr>
<td>B</td>
<td>251%</td>
<td>0%</td>
</tr>
<tr>
<td>CCC</td>
<td>4%</td>
<td>0%</td>
</tr>
</tbody>
</table>

Select Portfolio:
- Fund A

Select ESG Score:
- E

Select Weighing Scheme:
- Equal-Weighted

ESG data reflects 2015-12-01

ESG Score Color Chart:
- Green is good; Red is bad

Chart 2: Treemap of Securities

- Size corresponds to weight
- Color corresponds to overall ESG score

Pillar
- E: Energy Efficiency
- S: Product Safety & Quality
- G: Corp. Governance

Chart 3a)

- Score & Wt. of Top 10 ESG Contributors

Chart 3b)

- Score & Wt. of Top 10 Securities

Breakout: Sector-level Scores (click on scores to see underlying securities)

- Cons. Disc. Underwear
- Cons. Staples Underwear
- Energy Underwear
- Financials Underwear
- Health Care Underwear
- Industrials Underwear
- IT Underwear
- Materials Underwear
- Telecom Underwear
- Utilities Underwear
Polling Question #4

What is the biggest obstacle to achieving a greater level of sustainability disclosure to your investors in your organization?
Your Panelists

Janine Guillot
Director of Capital Markets Policy and Outreach, SASB

Robert Herz
Former Chairman, FASB.
Board Member of SASB, Workiva, Fannie Mae, Morgan Stanley

Rakhi Kumar
Head of ESG Investments and Asset Stewardship, State Street Global Advisors

Malcolm Ryerse
Director, Responsible Investment, Columbia Threadneedle Investments
Accounting for a Sustainable Future