SASB Press Kit

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The New York Times

A Good Corporate Accounting of Social Costs is Needed
By Jean Rogers
April 16, 2015

Source: http://www.nytimes.com/roomfordebate/2015/04/16/what-are-corporations-obligations-to-shareholders/a-good-corporate-accounting-of-social-costs-is-needed *(Retrieved 5/19/15)*

Corporate concern about issues like climate change, population growth or inequality is not just a matter of altruism, but of the company's growth and prosperity.

Insurance companies' insured assets are highly vulnerable to rising sea levels and intensifying storms. Credit card companies must walk a line between high returns and crippling debt for their customers. Coca-Cola, for example, can focus on social and environmental issues such as water quality, biodegradable packaging and obesity, not just because they are popular but because they can affect the company's financial future.

Sustainability factors can improve financial performance. The trick is identifying which factors affect the bottom line.

Research shows that stock prices of companies with an eye to more than just the bottom line did better than other companies if they focused on a subset of sustainability factors that actually improve financial performance. The trick is identifying which sustainability factors will make an impact to the bottom line.

And here's the hard part: These subsets of sustainability factors that influence financial performance differ by industry. Data security is critical to the success of IT companies. Greenhouse gas emissions affect oil and gas companies. Food safety matters to restaurants. The list continues. The Sustainability Accounting Standards Board is identifying which sustainability issues affect a company's bottom line in more than 80 industries.

Right now, investors who want to assess corporate performance on environmental, social and governance issues, are navigating with no map or compass. While a global survey found that 90 percent of institutional investors said that performance on these issues ''had played a pivotal role in their investment decision-making process,'' they don't have the information they need to evaluate their financial effects.

Just as the accounting industry set standards in 1972 for reporting financial information, we need accounting standards for sustainability factors such as energy consumption, fair labor practices, data security and supply chain management. Sustainability accounting involves defining metrics that fairly represent a company's performance. These are the standards that our board is providing.

Companies can't create long-term shareholder value without managing the sustainability factors that matter the most. Thus, the question isn't whether companies have to choose between profit and purpose. Companies can use sustainability to maximize profits as long as the sustainability factors have a financial impact.

THE WALL STREET JOURNAL.

The Environment and the Bottom Line
Jean Rogers of the SASB says investors need better information
By Jeffrey Ball
March 30, 2015

Source: http://www.wsj.com/articles/the-environment-and-the-bottom-line-1427773182 *(Retrieved 5/19/15)*

What kind of impact will environmental and social-governance issues have on the corporate bottom line? According to the Sustainability Accounting Standards Board, most companies currently don't account for such impacts in clear or comparable ways. If they did, the SASB argues, capital markets and investors would be better off.

To that end, the SASB, through research and by working directly with stakeholders, helps define what is likely to be material for a given company in a given industry and seeks to have that information reported to investors.

Jean Rogers, chief executive and founder of the SASB, discussed her group's work with Jeffrey Ball, contributing editor at The Wall Street Journal and scholar-in-residence at Stanford University's Steyer-Taylor Center for Energy Policy and Finance.

Edited excerpts follow.

MR. BALL: There are lots of advocates for these kinds of disclosures. Your sense is that this has led to a lot of glossy reports, but that people don't know what they're reading.

MS. ROGERS: There are many wonderful organizations who have raised awareness of these issues. We are focused like a laser on investors and capital markets and the narrow subset of information they need to make decisions about sector allocation or evaluation.

Climate is one of the most interesting of what we call crosscutting topics. But it doesn't manifest itself the same way, industry to industry.

MR. BALL: What should the health-care industry report?

MS. ROGERS: Their readiness and their business continuity processes, and how they manage disasters and increasing storms. I was just looking at some data from NYU [Langone] Medical Center, and they lost $1.2 billion just from that one storm [Hurricane Sandy].

MR. BALL: Oil and gas?

MS. ROGERS: In carbon-intensive industries you want to understand the greenhouse-gas-emissions intensity, the risk of regulation, risk of capital expenditures that may not be able to be brought to fruition. That's what we ask companies to disclose.

In banking, it's financed emissions and the carbon intensity of the portfolio.

Understanding greenhouse-gas emissions in every industry and company is useful from a policy perspective and understanding which industries to regulate. But from an investor's perspective, it doesn't tell you the risk that's embedded in your portfolio.

MR. BALL: By "financed emissions," you mean what sort of power plants a bank is financing in China and India?

MS. ROGERS: That's right. We have a metric that looks at the carbon intensity of the loans, and how they integrate these considerations into the financing they're doing prior to the loan.

MR. BALL: Who is doing well at this, who's not and why?

MS. ROGERS: Well, we read a lot of 10-Ks and actually 70% of the topics that we cover in our standards are addressed in some way in the 10-K, already in the mandatory filings, but with boilerplate information.

Companies say, "But investors aren't using what we're telling them." Well, that's because it's not decision-useful. More than half of that 70% is done with boilerplate statements.

We're trying to move the needle to high-quality disclosure using metrics on known trends and uncertainties that are related to how these issues affect the financial condition and the operating performance of the company.

Airlines are starting to talk about the impact on the operating budget. In airlines, fuel can be up to 40% of the operating costs. So understanding both conservation measures and how they're addressing alternative fuels, the R&D that's going into it, as well as the fuel-hedging practices, is very important. Fuel hedging can actually mask the need to conserve. It's a really good financial mechanism for financial risk, but it doesn't address the underlying environmental issue.

MR. BALL: To the extent that an airline hedges on fuel and therefore mitigates the effect of a rise in fuel price, it is masked from the financial need to improve its energy efficiency?

MS. ROGERS: Right, as long as you guess right [on the direction fuel costs go]. Because there's always the chance, as we've seen, that [the cost] goes down.

MR. BALL: Who's been tough to get to the table and why?

MS. ROGERS: We've had a tough time with the railroad industry. We've had a tough time with some transportation industries.

MR. BALL: Planes or cars or…

MS. ROGERS: A little bit of both. We've also had a tough time with banks and the financial industry. Those industries are highly regulated and may perceive what we're doing as regulation. But it's accounting infrastructure. The [Securities and Exchange Commission] Regulation S-K, there for eight decades now, says if information's material, you must disclose it to investors.

The things we're talking about are things companies are grappling with. The reason there's a risk factor, or a boilerplate statement, is because some securities lawyer in the company or in their external adviser has said, "We better say something about that." So the standard really just helps it to be useful to investors and hopefully also helps the companies begin to manage performance on the issue, which is where you derive value.

The Type of Socially Responsible Investments That Make Firms More Profitable
By George Serafeim
April 14, 2015

Source: https://hbr.org/2015/04/the-type-of-socially-responsible-investments-that-make-firms-more-profitable *(Retrieved May 19, 2015)*

One of the most contentious issues in business revolves around the role of for-profit companies in addressing social and environmental problems. Should a business be driving a "conversation" about race or pressuring U.S. states to reform discriminatory laws? And as investors inevitably ask, does engagement on such issues detract from generating profits?

The answer to that last question is no, according to a study we recently completed. We find that firms making investments and improving their performance on environmental, social, and governance (ESG) issues exhibit better stock market performance and profitability in the future. For companies, this suggests that their efforts to do good are rewarded. For investors, this suggests that there is substantial value from analyzing non-financial data and incorporating it into their decisions.

However, not all such initiatives are equally beneficial. My research, with Mozaffar Khan and Aaron Yoon, suggests companies should stick to social and environmental issues that are strategically important for their business if they want such efforts to contribute to the valuation. The results of this paper provide support to an earlier article ("The Performance Frontier: Innovating for a Sustainable Strategy") where we described a framework that companies could use to create value by doing good.

For instance, managing environmental impact is a very important element of business strategy for firms in the fossil fuel or transportation industries. Less so for financial institutions or healthcare companies. In contrast, fair marketing and advertising of products are very important for companies in these sectors. With this intuition we could hypothesize about the ESG investments that would be financially important for different industries, but until recently we had no objective and systematic way of making those judgments.

Our study was made possible because of data infrastructure that was created only recently by the Sustainability Accounting Standards Board (SASB). SASB develops industry-by-industry accounting standards that identify the material ESG issues that could have financial implications. SASB uses the U.S. Supreme Court's definition of material information as information 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." Going industry by industry, we hand-mapped the standards to data items that codify the investments that hundreds of companies in the US make each year over the last twenty years. (Interestingly, across industries, on average, only about 20% of the ESG issues were classified as material.) This allowed us to construct an index ranking companies based on investments on material issues and another index ranking companies based on investments in immaterial issues. Using models that control for other systematic risk factors (market, size, value vs. growth, momentum, and liquidity) we constructed portfolios of companies that score high in ESG investments versus those that score low.

The results are very consistent: firms making investments on material ESG issues outperform their peers in the future in terms of risk-adjusted stock price performance, sales growth, and profitability margin growth. In contrast, firms making investments on immaterial ESG issues have very similar performance to their peers suggesting that such investments are not value relevant on average.

Importantly, our study ruled out reverse causality – it is not the case that more profitable firms simply choose to invest more in ESG. We accounted for this by controlling for the correlation between the level of investments with current firm profitability, valuation, size, and financial leverage, and by examining stock price performance and implementing a trading strategy that any investor could implement in real time.

The results of our study suggest that companies need to analyze which ESG issues are strategically important to their business. Improving performance on those will likely lead to better financial performance in the future. At the same time, they need to be able to inform their investors how they are performing on those issues by communicating credible key performance indicators. In turn, investors need themselves to analyze what are the important ESG issues for the companies in their portfolio and manage hidden risks. Not all social and environmental initiatives are created equal. But if companies stick to the ones most related to their businesses, they can drive social and financial performance simultaneously.

THE WALL STREET JOURNAL.

Sustainability Accounting for Investors: Q&A with Robert H. Herz
By Gregory Millman
February 19, 2015

Source: http://blogs.wsj.com/riskandcompliance/2015/02/19/sustainability-accounting-for-investors-qa-with-robert-h-herz/ *(Retrieved: May 19, 2015)*

Robert H. Herz served as chairman of the Financial Accounting Standards Board from 2002 through 2010. In January of this year, he joined the board of the Sustainability Accounting Standards Board, an organization working to develop industry-specific environmental, social and governance accounting standards for investment analysis. Mr. Herz has spent much of his career studying non-financial metrics relevant to value creation, and in 2001 co-authored a book on the subject, entitled The ValueReporting Revolution: Moving Beyond the Earnings Game. In a conversation with Risk & Compliance Journal, Mr. Herz explained why and how he expects to see adoption of such standards.

What is sustainability accounting?

Mr. Herz: The SASB aims at producing metrics on key sustainability issues that impact company performance over time. This reporting is for investors, not aimed at the broader group of people interested in corporations from an ESG point of view, but rather at providing a set of information on ESG issues that matter from an investment point of view.

How do you develop such standards?

Mr. Herz: You've got to do it industry by industry, because in a particular industry or sector, some issues matter more than others. For example, in service and some types of manufacturing industries, labor policies matter an awful lot. With services it's being able to attract and retain the best people. In manufacturing, you get to the issues of child labor overseas and things like that. In some industries, the key issues are environmental, for example related to carbon emissions. What the SASB does is research which issues in the array of all ESG issues seem to matter most to a particular industry and its value proposition. Then comes a thorough due diligence process to develop metrics that capture those key issues.

How would the metrics be used?

Mr. Herz: The idea is to develop standardized metrics across an industry so companies can benchmark themselves and investors can benchmark them. They are non-financial metrics but they are metrics that drive financial performance and answer the question, "If I were going to make a big investment or buy a company, what would I look at besides the financial statement?"

For example, in the pharmaceutical industry, it might be the proportion of your business from new products aimed at improving health and welfare. Unilever has had a whole initiative the last five years to grow their line of products in that area and it now constitutes a significant and fast-growing part of their revenue. The counter example would be pharmaceutical products that cause lots of adverse side effects beyond the benefits, have been taken off the market, and similar matters.

What have investors had to say to you about such metrics?

Mr. Herz: What I hear from investors is that they are very interested in these issues but they have to sift through so much data that is unstandardized, not comparable, aimed at a broader social responsibility

community. They've been saying that if they could have a set of more standardized metrics, targeted at the issues that really matter to a particular industry, that's what they want. They don't care very much about the carbon emissions of an investment bank for example; it is not key to their investment thesis, but for a utility it probably is.

Do you expect a regulatory push for this disclosure?

Mr. Herz: My view is that it has to be market-driven to begin with, driven by investor pull, and by companies seeing the advantage of doing it.

What stage of development are the standards now and what is the timeframe for adoption?

Mr. Herz: The SASB is well into issuing provisional standards, and once they finish that there's going to additional due process, including talking to people industry by industry, then finalizing. There's been a lot of interest. A number of these metrics are already reported by companies in their sustainability reports and other venues, but not in as targeted a way. I would hope to get to a broad expectation of such disclosure by the market within five years. A lot of companies are intrigued but cautious; there are always questions of whether it exposes me to more legal risk, do I really want to be first, those kinds of questions.

Why is such disclosure important?

Mr. Herz: I'm not a tree hugger or an environmental activist. I've devoted a lot of my career to provide better information to help the capital markets work. I believe that what you measure matters and how you report it matters and that this is important to the investment analysis.

COMPLIANCE WEEK
THE LEADING INFORMATION SERVICE ON CORPORATE GOVERNANCE, RISK AND COMPLIANCE

Why Boilerplate Battles Continue to Rage
By Joe Mont
February 10, 2015

Source: https://www.complianceweek.com/news/news-article/why-boilerplate-battles-continue-to-rage#.VPTfhS4kWH8 *(Retrieved May 19, 2015)*

Time and time again, with both guidance and comment letters, the Securities and Exchange Commission has urged companies to avoid using "boilerplate" language in their disclosures.

One might even call the SEC's pronouncements boilerplate warnings, since they agency makes them all the time—and companies never seem to embrace the message.

"It's an interesting tension," says Bree Archambault of the law firm Reed Smith. "When you are working on disclosure documents, there are specific disclosures you are required to make and some of it does not change a lot from year to year. If it has passed muster in past years, the situation is still the same, and the business is generally the same—run in the same way with the same segments—the company has an incentive not to change that language."

Jean Rogers, founder and CEO of the Sustainability Accounting Standards Board, goes even further: "There is an extraordinary amount of boilerplate disclosure across topics and across industries," she says. SASB recently reviewed companies' sustainability-related disclosures, and flagged nearly half as boilerplate.

"There is a problem with going too far in your disclosure, but there is also a problem with not going far enough," Rogers says. "We see people erring on the side of not going far enough and relying on boilerplate."

While the SEC admonishes boilerplate language, companies are challenged by a lack of uniform definition for what exactly boilerplate is. Determinations of materiality, especially about what an investor would want, are typically left to the issuer. Nearly any choice could be debated and challenged.

The prevalence of boilerplate language is "a manifestation of companies recognizing their risk factors, but not having standards or guidance on how to actually disclose them better," Rogers says. "You have U.S. Generally Accepted Accounting Principles for financials; the Financial Accounting Standards Board does a really good job with how to disclose financial performance, but there really is very little more than *ad hoc* guidance from the SEC on how to look at non-financial or special topics that are material. How do you address them?"

Cyber-security disclosures are the latest target for the boilerplate debate. How bad must a breach be to warrant disclosure in a Form 8-K? Should that determination be based on the number of consumers affected, the financial toll, or degree of media attention?

In 2011 the SEC's Division of Corporation Finance did outline items that companies must consider when identifying specific business risks caused by cyber-security incidents. Among them: how those costs might affect the balance sheet; the correlation of those risks to the company's business model; possible

legal proceedings; and how to make appropriate financial statement disclosure to reflect the effect of a cyber-attack.

Regulation S-K, which governs disclosure in Form 10-K filings, requires companies to disclose material information that is a risk factor or likely to affect financial condition or operating performance. “Even when [the SEC] issued guidance on a particular topic like cyber-security, conflict minerals, or climate change, what they are really doing is interpreting S-K,” Rogers says. “The SEC tends to not get specific or raise questions about how far companies should go to determine what material is.”

The latitude given companies is problematic, critics say. “The traditional approach is to let companies assess their own cyber-risk factors, which is the equivalent of letting the chickens decide how tasty they are, or aren’t, to the fox,” says Jeffrey Carr, a cyber-security analyst and CEO of Taia Global.

Vague vs. Material

Carr cites Sony’s response to breaches over the years as an example of overly broad 10-K disclosures. After Sony’s high-profile hacker attack last November, Carr looked at the company’s cyber-risk disclosures since 2011. The language “remains pretty much the same” over the years, he says. “This is pretty generic stuff that doesn’t contain anything specific to Sony that wouldn’t apply to every other public company.”

The current crop of cyber-security disclosures “are effectively worthless from an investor’s point of view,” Carr says. “There is a false argument that you can’t expect them to inform the bad guys about weaknesses in the network. That’s not what is being asked for. The SEC doesn’t want the company to say it is vulnerable to a SQL injection, or spear fishing, or whatever. They simply want an assessment of risk.”

The unwillingness to advance beyond boilerplate cyber-security disclosures ties to “whether or not they are disclosing something that would put them at a competitive disadvantage,” Rogers says. “Companies don’t want to be at the risk of omitting material information, so they put in a boilerplate statement.”

SASB is currently working with a cross-section of industries to develop voluntary standards for cyber-security and environmental disclosures that companies can use. “Companies appreciate having a standard that helps them know exactly how far they should go when talking about this issue, and a standard can help level the playing field,” Rogers says. “They need to provide decision-useful information to investors, and boilerplate doesn’t cut it.

A similar push is underway by Ceres, a coalition of investors and public interest groups. Its beef is with a 2010 SEC requirement that companies disclose the material effects of climate and environmental change, and the effects of related pending legislation and regulation, on their business operations. The SEC, Ceres says, “is not adequately enforcing” compliance, and companies, in turn, are ignoring the requirement.

Roughly 40 percent of companies in the S&P 500 do not make any climate-related disclosure in their 10-K filings, a recent study by Ceres found. Among those that do, “the majority of financial reporting on climate change is too brief and largely superficial.” Ceres is demanding that the SEC do a much better job enforcing those requirements.

How the SEC will react to such pressures remains to be seen. While environmental issues may not inspire much attention beyond activist shareholders, cyber-risk certainly does.

Since its 2011 cyber-risk guidance, CorpFin has issued comments to fewer than 100 companies about their related disclosures. When it does intervene, SEC staff often demand specific information.

In 2012, when the Amazon subsidiary Zappos was breached, Amazon referred in its next periodic filing only to the potential of a cyber-attack that “could expose us or our customers to a risk of loss or misuse of information, adversely affect our operating results, result in litigation or potential liability for us, and otherwise harm our business.” The SEC protested and demanded specific detail rather than vagaries. Amazon protested, but eventually acquiesced.

ConocoPhillips, in its 2012 annual report, mentioned only the phase “cyber-attacks” in its listing of potential risks. The SEC and the company tangoed for several weeks over how much additional detail CorpFin wanted included. Conoco eventually added language to indicate that several “non-material breaches” had occurred.

The SEC may soon consider more prescriptive disclosure requirements. Chairman Mary Jo White has hinted as much in public comments. Various members of Congress have called for the same, and that push gets stronger with each new high-profile breach.

The SEC’s current budget appropriation may be the tipping point. The 2015 Omnibus Appropriations bill passed by Congress in January included a rider demanding that the SEC review and “modernize” cyber-security disclosures.

BUSINESS LAW TODAY

Sustainability Reporting: The Lawyer's Response
By Nancy S. Cleveland, David M. Lynn, Stephen A. Pike
January 2015 Issue

Source: http://www.americanbar.org/publications/blt/2015/01/04_pike.html *(Retrieved 5/19/15)*

With ever-increasing frequency, clients are seeking advice about reporting and communication on sustainability issues. "What are we legally required to communicate?" "What are we permitted to communicate?" "What can or should we say to stay competitive and protect business relationships, profitability, and our social license to operate?" "What standards should we use?" This article will help lawyers understand and advise clients on their sustainability communications pressures and needs.

Corporate sustainability is a business management practice. When used strategically, it enhances business value. As a practice, it involves assessing and managing risks and opportunities that arise from environmental, social, and economic impacts of the company and its industry. Assessment is done for short-, medium-, and long-term time horizons. This broader and longer-term perspective is essential to realizing value from sustainability management.

As a practical matter, the concept of sustainability management may conflict with some aspects of current corporate law and behavior. These conflicts can be generalized by the reality that most of corporate America focuses on a market-imposed, short-term, single bottom line. But the marketplace is in flux. Perspectives are changing in response to climate change, population growth, constrained resources, globalization of supply chains, and more transparent and ubiquitous communications. The upshot is growing pressure on businesses to evolve toward a triple bottom line approach: considering social, environmental, and economic impacts over a longer term, and their implications for governance. As lawyers, we will be called upon to help navigate these shifting influences on business management and success.

What's Going On?

Macro Drivers for Sustainability Reporting Pressure

The drivers that are creating pressure on companies to address and communicate more and more about sustainability issues arise from a number of factors, including from a variety of external and internal stakeholders. There are four primary macro drivers that have had, and will continue to have, wide-ranging social, environmental, and economic impacts with the potential to affect businesses everywhere. Being attuned to, and mitigating the risks of, or adapting to those impacts is a key attribute of a sustainable company.

Concern about climate change and greenhouse gas emissions: Rising levels of greenhouse gasses in our atmosphere are driving increases in average temperature on the planet. This warming leads to changes in our climate and natural systems, resulting in sea level rise, droughts, floods, severe weather, wildfires, and ocean acidification. Even 2°C of warming will have a significant adverse impact on human health and well-being.

Population growth and resource constraints: World population is on track to reach 9 billion by 2050 and 10 billion by 2100. The global middle class is expected to triple by 2030. At today's pace, global energy

demand will increase by 57 percent over the next 25 years. Water use is expected to increase by 50 percent in developing countries and 18 percent in developed countries by 2025. Our current level of consumption utilizes 1.5 Earths to provide resources to meet current demand and absorb waste. These factors will drive prices of all commodities up and lead to serious problems without corrective actions and creative solutions. Businesses have significant risks and opportunities in this respect. *See*, World Business Council on Sustainable Development; Energy Information Agency; Geo-4 – Global Economic Outlook; Global Footprint Network.

Organizational and global interdependence: Large companies used to have several hundred partners and suppliers; today they have thousands, and they are spread across the globe. Companies of all sizes are outsourcing noncore functions, partnering for some core functions, and building larger business networks in general. The greater the number of outside suppliers and service providers upon which a company relies, the more difficult it is to manage the associated risks across multiple geographies. This is true from both a supply chain and reputation management perspective.

Social license and accountability to stakeholders: Public demand for transparency and accountability has increased markedly. An instant information society has emerged from widespread access to social media, the Internet, and cable news. A single individual now has the ability to communicate instantaneously and globally to influence public opinion on a topic or a business. Multiplicities of stakeholders are affected by and interested in how a company manages sustainability issues. Consumers and investors are increasingly factoring a company's ethics, sustainability, and social responsibility into their buying and investment decisions.

Stakeholder Perspectives

Sustainability reporting serves the needs and interests of a wide and growing variety of stakeholders, ranging from investors, employees, customers, and suppliers, to governments, regulators, local community groups, and nongovernmental organizations. Stakeholder reasons for seeking information on sustainability issues, the information they seek, and the lens through which they view the reported information varies. The number and variety of information requests about environmental, social, and governance (ESG) activities is a significant burden for many companies. Accordingly, companies must balance how and to whom they respond.

Investors and customers are the two stakeholder groups that garner the most attention. Companies are influenced by their own investors to pursue sustainability into their supply chains. As a result, understanding what is driving the investment community to care about sustainability activities and reporting is key.

In many cases, institutional investors care about medium- and long-term value and whether the companies in which they invest are contributing to systemic problems or are conducting their business in a way that helps solve those problems. This is not to say that short-term financial returns are unimportant to institutional investors, but rather, that more and more institutional investors are taking into account a broader range of factors in their investment decisions. Company performance on ESG factors are being included because they are outperformance indicators. Robert G. Eccles, Ioannis Ioannou, and George Serafeim, *The Impact of Corporate Sustainability on Organizational Processes and Performance*, first published November 01, 2011 (dated 11/23/11). In the words of Thomas P. DiNapoli, New York State Comptroller and Sole Trustee of the New York State Common Retirement Fund: "Our goal is simple: we want long-term sustainable economic growth. And we have found from experience that comprehensively integrating environmental, social and governance considerations into the investment process is essential to achieving that goal." Peter Ellsworth and Kirsten Snow Spalding, *The 21st Century Investor: Ceres Blueprint for Sustainable Investing*, 2013, Forward, www.ceres.org.

Pressures to Report; Understanding the Reporting Landscape

Clients are measuring their reporting against that of their peers and competitors. They are gauging social pressure to demonstrate responsible corporate behavior. There have been significant reporting developments, both in terms of the growth in reporting and the number and quality of reporting requirements, standards, or frameworks.

The arguments for not reporting are shrinking day after day for companies that have yet begun to report on their sustainability progress. Now that 53% of the S&P 500 and 57% of the Fortune 500 are reporting on their Environmental, Social, and Governance impacts, the non-reporters are now in the minority. We believe this minority will continue to shrink as it has in the past few years. The benefits of sustainability reporting will become increasingly obvious as more time passes and the long term benefits are easier to measure.

Governance & Accountability Institute, Inc., *2012 Corporate ESG/Sustainability/Responsibility Reporting, Does It Matter?* (Dec. 15, 2012).

Making Reporting Decisions

Once a company decides to report to stakeholders about its sustainability activities, risks, and opportunities, legal questions arise. Public-facing information about sustainability often starts as a marketing initiative in response to customer interest or as a means of demonstrating social responsibility and philanthropy. This type of information can then become the basis of requests to "verify" information gathered by a rating systems that will report with or without company input or corrections. Other reporting systems, like the CDP (formerly the Carbon Disclosure Project), will request formal reporting and publicize a failure to respond or report. As soon as investors or rating systems get involved, or customer pressure takes the form of supply chain requests, the focus rapidly shifts from a marketing effort. Management begins to ask what the company is legally required to report and what the company should report to support reputation, stakeholder relationships, and business development.

Mandatory Reporting Requirements

1. SEC Filings.

Companies subject to the Securities and Exchange Commission (SEC) filing requirements must disclose material information in their SEC filings, such as the Form 10-K. Various rules and regulations, including Regulation S-K, may require the disclosure of material sustainability information in the Form 10-K and other periodic SEC filings, depending on the circumstances. Securities Act Rule 408 and Exchange Act Rule 12b-20 require a registrant to disclose, in addition to the information expressly required by line-item requirements, "such further material information, if any, as may be necessary to make the required statements, in light of the circumstances under which they are made, not misleading."

Over the past several years, the SEC has struggled with how best to address evolving concerns with climate change and sustainability in the agency's disclosure requirements. The SEC attempted to address the issue of climate change by publishing an interpretive release providing specific guidance as to how existing rules may require disclosure of information relevant to climate change. Release No. 33-9106, *Commission Guidance Regarding Disclosure Related to Climate Change* (February 2, 2010). The interpretive release identifies how climate change disclosures may be required under particular disclosure items in Regulation S-K, depending upon a company's circumstances. These disclosure items include Description of Business
(Item 101 of Regulation S-K), Legal Proceedings (Item 103 of Regulation S-K), Risk Factors (Item 503(c) of Regulation S-K), and Management's Discussion and Analysis of Financial Condition and Results of Operations (Item 303 of Regulation S-K). The principles that the SEC articulated in the climate change interpretive release can be applied in other contexts related to sustainability in determining if a public company has any disclosure obligations with respect to such matters.

The SEC's interpretive release addresses four topics that companies should consider when evaluating the need for, and appropriate level of, disclosure related to climate change matters:

- The impact of legislation and regulation regarding climate change, including the potential impact of pending legislation.
- When material, the impact on their business of treaties or international accords relating to climate change.
- Whether legal, technological, political, and scientific developments regarding climate change will create new opportunities or risks, including reputational risks.
- The actual and potential material impacts of the physical effects of climate change on their business, such as the effects of severe weather, sea levels, arability of farmland, and water availability and quality.

In other sustainability areas, Congress has recently amended the federal securities laws to impose disclosure obligations regarding certain types of human rights and other issues of interest to specific groups. Recent examples include disclosure regarding the sourcing of certain "conflict minerals" (Section 13(p) of the Securities Exchange Act of 1934 ("Exchange Act"), which was implemented by the SEC by rule), payments to governments by resource extraction issuers (Section 13(q) of the Exchange Act, which is in the process of being implemented by SEC rule), and business with certain governments, persons, and entities subject to specific U.S. trade sanctions (Section 13(r) of the Exchange Act, which was effective upon enactment).

2. State and Local Requirements.

Other requirements for reporting on sustainability issues may arise at the state or even local level, or come into play by virtue of the geographic scope of a company's business. For example, the California Transparency in Supply Chains Act requires every retail seller and manufacturer doing business in the State of California and having worldwide annual revenues of $100 million or more to disclose their specific actions to eradicate slavery and human trafficking in their direct supply chains for tangible goods offered for sale.

For a regulatory example, the insurance commissions in six states (California, Connecticut, Illinois, Minnesota, New York, and Washington) require insurance companies with direct written premiums of $100 million or more in their state to complete an annual climate risk disclosure survey.

3. International Requirements.

In spring 2014, the European Parliament passed a law requiring publicly traded companies with more than 500 employees to report on nonfinancial sustainability factors. The law will go into effect in 2017, and will require nearly 7,000 companies to include this new information in their annual financial reports – 4,500 more than are doing so today. The new law requires affected companies to report on ESG factors, including human rights impacts, diversity, and anticorruption policies. Companies will be expected to describe their business model and the outcomes and risks of their policies. Companies will also be required to include their supply chain in reporting. This will likely have a trickle-down impact, forcing smaller and medium-sized private companies and multinational companies upstream in the value chain to report even though the law does not apply them.

Under Canadian securities laws, public companies must disclose all material information, including material information about environmental and social issues, and there are additional disclosure obligations under the TSX and TSX Venture Exchange timely disclosure policies.

In October 2010, the Canadian Securities Administrator published Staff Notice 51-333, Environmental Reporting Guidance to provide guidance on continuous disclosure requirements relating to environmental matters under applicable Canadian securities laws and to assist issuers in determining what information

about environmental matters needs to be disclosed and about enhancing or supplementing their environmental disclosures. The staff notice was motivated by the impact of environmental matters on reporting issuers, the changing regulatory landscape, and increasing investor interest in environmental matters.

Quasi-Voluntary and Voluntary Reporting

There are many stakeholder and other organizations that pressure companies for ESG information. Among the many means used to gather this information are a myriad of investment screening tools, rating organizations, and reporting frameworks that aggregate public information or provide vehicles for sustainability reporting. Below is a brief overview of the most prominent among these organizations, tools, and reporting frameworks.

Investors use ESG screening to measure or assess how a company manages social and environmental impacts. This screening focuses on whether a company identifies and either mitigates risks or seizes opportunities with respect to ESG indicators.

Investment screening tools are flourishing:

- The Bloomberg ESG Valuation Tool and its ESG Score has experienced significant interest. This tool "enables users to apply a financially-based methodology to assess and value the impact of ESG factors on a company's Earnings Before Interest and Taxes (EBIT) performance and share price." PWC, *Do Investors care About Sustainability? Seven Trends Provide Clues* (March 2012).
- MSCI has several screening tools/indices, including its ESG Impact Monitor.
- FTSE4Good revamped and expanded its screening process. Companies are required to publicly disclose a broad array of sustainability information to gain and maintain listing on the index.
- GS SUSTAIN is another index that incorporates ESG into its analysis. Like MSCI and FTSE4Good, GS SUSTAIN submits information it has gathered from the public realm for company review, correction, and supplementation.

The CDP, a global not-for-profit organization, operates a reporting framework and rating system. The CDP holds the largest and most comprehensive collection of primary climate change, water, and forest-risk information. Investors representing more than a third of the world's capital request corporate accountability on climate change through the CDP reporting framework.

Global Reporting Initiative (GRI) is the globally-recognized "gold standard" for sustainability reporting. The framework includes reporting guidelines and sector/industry guidance. It requires a high degree of organizational transparency and accountability. The uniform indexed reporting structure provides stakeholders a capacity for year-over-year analysis and easy comparison of reports from different companies. When investors pressure companies to report, they most often request reporting using the GRI framework.

On the leading edge of the reporting industry, and in support of an emerging interest in integrating financial and non-financial reporting, the International Integrated Reporting Council (IIRC) has developed the Integrated Reporting Framework. This includes guidance for how publicly traded companies can integrate sustainability into their annual reports so that the public can understand the value of sustainability initiatives and can effectively compare one company to the another. The stated purpose of integrated reporting is to show how a company creates value of the short, medium, and long term. http://www.theiirc.org/resources-2/faqs/.

Voluntary Standards to Support Mandatory Reporting

The Sustainability Accounting Standards Board (SASB) is developing voluntary standards, which identify industry-specific, sustainability-related issues that may give rise to material information for companies to disclose. The intent is for companies to reference the standards as a guide when making sustainability disclosure decisions for mandatory filings to the SEC. The complete set of guidelines is scheduled for release in early 2016. *See* www.sasb.org. The SEC has not acted on incorporating the SASB standards into any disclosure requirements.

The Lawyer's Response

The manner in which sustainability issues are reported or communicated to stakeholders and others must align with the type and purpose of the report or communication. Mandatory reporting should follow SEC or other governing requirements. Voluntary reporting should, on its face, be readily distinguishable from such mandatory reporting. Lawyers should recommend that language be used that reflects the standard and the audience for the reporting venue. Counsel will need to weigh litigation risks that voluntary reporting may carry for reported information that is significant, but not material, and therefore not included in mandatory reporting.

This is of primary significance because of the ways in which differing concepts of materiality are incorporated into mandatory and voluntary reporting requirements:

- Under the GRI reporting framework, information is considered material and should be included in a report if it "may reasonably be considered important for reflecting the organization's economic, environmental and social impacts, or influencing the decisions of stakeholders."
- The IIRC deems information to be material if "it is of such relevance and importance that it could substantively influence the assessments of providers of financial capital with regard to the organization's ability to create value over the short, medium and long term."
- For SEC reporting purposes and under the voluntary SASB standards, information is deemed to be material if there is "a substantial likelihood" that a "reasonable investor" would view the information as "significantly alter[ing] the 'total mix' of information made available." *TSC Indus. v. Northway, Inc.*, 426 U.S. 438, 449 (1976).

Disclosures under the U.S. federal securities laws are a mixed question of law and fact. The SEC has noted that the issuer is in the best position to know what is likely to be material to investors. "[A] corporation is not required to disclose a fact merely because a reasonable investor would very much like to know that fact." *Richman v. Goldman Sachs Group, Inc.*, *et al.*, 10 Civ 3461 (June 21, 2012, United States District Court for the Southern District of New York).

Companies are required to disclose material information only where the federal securities laws or other applicable legislation specifically impose such a duty to disclose. The analysis should focus on whether or not the information is material by securities law standards and whether there is a prima facie duty to disclose the information.

Because a number of recognized standards for sustainability reporting outside of the SEC's disclosure requirements reference different concepts of "materiality," counsel must be cognizant of those varying definitions while remaining focused on the specific duties and obligations that are currently contemplated by the U.S. federal securities laws. Understanding these nuances enables lawyers to help clients clearly identify the importance ascribed to information by reference to the standard and audience. For example, a company could use the concept of materiality for investor-related information that is included in required reporting to the SEC. Other information should be identified using words like "significant," "important," or "key," or as being relevant to stakeholders other than investors. The company could add disclaimers or cautions where appropriate.

All reporting standards require that a company's sustainability disclosures − even where there is no duty to disclose under the U.S. federal securities laws – be both accurate and complete. To effectively manage

sustainability reporting and communication, companies must build appropriate reporting capacity (including disclosure controls and procedures) to identify and vet sustainability issues. The development and implementation of sustainability management systems will serve to provide a company with a process for measuring, monitoring, and improving sustainability reporting and performance. These systems should encompass an internal educational component to ensure awareness of sustainability activities and reporting needs.

Companies ask their lawyers to review mandatory reporting disclosures as a matter of course. Given the complexity of sustainability issues, there is also a role for lawyers in reviewing and advising on voluntary reporting. Counsel should help clients weigh liability risks against reputational, relational, and other benefits of voluntary reporting. Understanding the drivers for that reporting noted above should guide that review and inform giving advice that protects client interests, while enabling them to respond to real and significant social and business pressures.

Bloomberg BNA

As the World Turns, So Must Its Markets
By Aulana Peters and Elisse Walter
September 22, 2014

Source: http://www.sasb.org/wp-content/uploads/2014/09/PDF_SASB-BBNA.pdf *(Retrieved: 5/19/2015)*

It's been roughly 2,500 years since the Greek philosopher Heraclitus observed that our universe's only constant is change. By comparison, a scant 72 have passed since Austrian-American economist Joseph Schumpeter coined the phrase "creative destruction" to describe the process through which capitalism perpetually reinvents itself. The similarities between these insights are unmistakable and instructive. Like Heraclitus' river, our economy flows ever onward; driven by innovation and fueled by free-market forces, it revolutionizes itself from within.

In today's world, management of risks and opportunities not reflected in financial statements influences corporate success. In fact, mega-trends like population growth, climate change, and resource constraints can and do have a profound effect on business outcomes. For example, insurance companies must identify the vulnerability of their insured assets to rising sea levels, increasing drought, and more severe winters. Hardware companies must consider how to source minerals from unstable regions where mining can fuel conflict. Credit card companies must consider how to protect against data breaches. These are just a few examples of how these trends already affect business outcomes and consequently must affect financial reporting. This is a natural evolution and one already recognized by investors who are requesting information on such issues as how a company is prepared for the potential challenges and opportunities presented by resource constraints, climate change, population growth, and emerging markets.

The dynamic of a changing world and changing investor focus is perhaps most readily apparent in our financial markets, where the difference between the book values listed on balance sheets and the market values reflected in stock prices grows wider each year. In 1975, only 17 percent of the assets in the S&P 500 were intangible; in 2010, the number was 80 percent.[1] When market valuations are increasingly based on intellectual capital, market share, brand value, and other "soft" assets that create shareholder value in a knowledge-driven economy, traditional financial statements tell only a part of the story. This point has long been acknowledged by the Financial Accounting Standards Board (FASB).[2] Investors are looking beyond financial statements, to environmental, social, and governance (ESG) issues and other concerns that are particularly relevant to investors in an economy dominated by intangible assets.

It is in the context of this shifting economic landscape that we are compelled to respond to an Aug. 4, 2014, Securities Regulation & Law Report article entitled "The Sustainability Accounting Standards Board, Insurance Companies and the SEC," which misapprehends SASB's goals and purpose and misconceives SASB's approach and methodology. To be clear, we share the authors' deeply held conviction that "excluding material information from the market does not improve market efficiency."[3] Nevertheless, we are equally convinced that the information that is "material" to investors—much like the world around it—is rapidly changing (indeed, has changed). In today's world, investors need and are demanding both financial statements and other material information to make informed decisions.

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[1] Ocean Tomo, Components of S&P 500 Market Value (2010), available at http://www.oceantomo.com/productsandservices/investments/intangible-market-value.
[2] FASB Business Reporting Research Project, Improving Business Reporting: Insights into Enhancing Voluntary Disclosures (Jan. 29, 2001), available at http://www.fasb.org/brrp/brrp2.shtml.
[3] "The Sustainability Accounting Standards Board, Insurance Companies and the SEC," by Samuel P. Gunther, Richard H. Murray and Sheila A.S. Gunther, Bloomberg BNA Securities Regulation & Law Report (Aug. 4, 2014) [hereinafter SASB, Insurance Companies and the SEC].

The Legal Basis for Sustainability Disclosures

Regulation S-K, as prescribed under the Securities Exchange Act of 1934, lays out the reporting requirements for SEC filings by corporate issuers and already requires companies to disclose material information on the Form 10-K. Pursuant to Item 303, companies are required to disclose their financial condition and results of operations, and to provide management's view on known trends or uncertainties that are reasonably expected to have a material impact on liquidity, capital, sales, revenues, or income.

The materiality of a fact is defined by the U.S. Supreme Court[4]:

> "There must be 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."

This definition of materiality has a singular and unwavering focus on the reasonable investor's decision to buy, sell, or hold a security.

A determination of materiality may be complex. In Staff Accounting Bulletin No. 99—Materiality, the SEC states that companies should not rely on financial thresholds or rules of thumb to make ultimate materiality determinations. For example, the Bulletin rejects the rule of thumb that a misstatement or omission of less than five percent is not material.[5] Instead, the Bulletin states that "an assessment of materiality requires that one views the facts in the context of the 'surrounding circumstances,' as the accounting literature puts it, or the 'total mix' of information, in the words of the Supreme Court." In other words, one must "consider both 'quantitative' and 'qualitative' factors in assessing an item's materiality."[6] This interpretation is supported by auditors' professional standards, which state that "materiality judgments are made in light of surrounding circumstances and necessarily involve both quantitative and qualitative considerations."[7]

Rising Investor Demand for Sustainability Disclosures

As investors increasingly recognize the financial impact of factors not reflected in financial statements, their demand for this information is growing. A recent global survey of institutional investors found that, during the past 12 months, assessment of performance on ESG issues "had played a pivotal role in their investment decision-making process" for 90 percent of the responding investors.[8] The report concluded that analysis of these issues "can no longer be dismissed as a niche approach to investment."[9]

While investor demand for information in addition to that contained in financial statements is rising, the availability and quality of this information needs improvement. Investors are engaging in fairly unproductive and costly means to get the information they need—89 percent of global institutional investors[10] responding to another recent survey say they will request sustainability information directly from the company, and 50 percent report they are "very likely" to sponsor or co-sponsor a shareholder

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[4] TSC Industries, Inc. v. Northway, Inc. (426 U.S. 438, 449, June 14, 1976), available at http://caselaw.lp.findlaw.com/scripts/getcase.pl?navby=CASE&court=US&vol=426&page=438 [hereinafter TSC].
[5] Securities and Exchange Commission, 17 CFR Part 11, SEC Staff Accounting Bulletin No. 99 – Materiality (August 11, 1999), available at http://www.sec.gov/interps/account/sab99.htm.
[6] *Ibid.*
[7] American Institute of Certified Public Accountants, AICPA Professional Standards, AU § 312.10 (2013), available at http://www.aicpa.org/Publications/AuthoritativeStandards/Pages/AuthoritativeStandards.aspx.
[8] Survey respondents represented large financial institutions such as third-party investment managers, banks, pension funds, foundations, endowments, sovereign wealth funds, insurance companies, and family offices. Fifty-nine percent of respondents worked for institutions with more than $10 billion in assets under management.
[9] EY, Tomorrow's investment rules: Global survey of institutional investors on non-financial performance (2014), available at http://www.ey.com/Publication/vwLUAssets/EY-Institutional-Investor-Survey/$File/EY-Institutional-Investor-Survey.pdf.
[10] Survey respondents represented asset managers, pension funds, and other types of institutional investors with combined assets under management of more than $7.6 trillion.

proposal.[11] Significantly, two-thirds of these investors say that they would be more likely to consider this type of information when making investment decisions if common standards were used.[12] In order to use such information, investors need complete data sets and comparable data they can use to benchmark and compare companies. Enabling the production of such data and benchmarks is what SASB does.

A Market-Driven Response

The Sustainability Accounting Standards Board was created to fill the market need for standardized disclosure of sustainability information. SASB's mission is to develop and disseminate sustainability accounting standards that help publicly listed corporations disclose material factors in compliance with SEC requirements.

SASB standards follow the U.S. Supreme Court's definition of material information, defined 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."[13] They provide a model for reporting material sustainability factors in the MD&A section of the Form 10-K, which "shall focus specifically on material events and uncertainties known to management that would cause reported financial information not to be necessarily indicative of future operating results or of future financial condition. This would include descriptions and amounts of (A) matters that would have an impact on future operations and have not had an impact in the past, and (B) matters that have had an impact on reported operations and are not expected to have an impact upon future operations."[14] Companies can voluntarily use SASB standards to help them comply with Regulation S-K, to meet the SEC-required disclosure obligation found in the MD&A, and provide management's view of their company's future prospects. This is wholly consistent with SEC guidance on the purpose of the MD&A,[15] contrary to suggestions that ESG information does not belong in the MD&A[16] and that disclosures made according to SASB standards "directly encroach on the domains of the FASB and the SEC."[17]

As a private sector body, SASB does not and cannot require disclosures or mandate disclosure standards, nor does it purport to do so. Rather, SASB develops standards that assist companies in fulfilling *existing* regulatory requirements *as they deem necessary*. However, the final determination of materiality is the onus of the corporation—this is consistent with the Supreme Court's explanation that the determination of materiality is an "inherently fact-specific finding."[18] Moreover, SASB is in direct periodic communications with the SEC, the FASB, the PCAOB, and others concerned with the regulation of financial disclosures to ensure that its activities support the SEC's authority to prescribe and enforce disclosure standards.

SASB standards are rooted in evidence, informed by industry expertise, and shaped by consensus. The standards development process begins with a three-month research phase. Evidence of investor interest

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[11] PwC, Sustainability goes mainstream: Insights into investor views (2014), available at http://www.pwc.com/en_US/us/pwc-investor-resource-institute/publications/assets/pwc-sustainability-goes-mainstream-investor-views.pdf.

[12] *Ibid.*

[13] TSC.

[14] 17 CFR § 229.303, Regulation S-K, Item 303(a) Management's discussion and analysis of financial condition and results of operations, available at http://www.gpo.gov/fdsys/pkg/CFR-2011-title17-vol2/pdf/CFR-2011-title17-vol2-sec229-303.pdf.

[15] See, for example, Interpretation: Commission Guidance Regarding Disclosure Related to Climate Change, Securities and Exchange Commission, 17 CFR Parts 211, 231 and 241 (February 2, 2010), Interpretation: Commission Guidance Regarding Management's Discussion and Analysis of Financial Condition and Results of Operations, Securities and Exchange Commission, 17 CFR Parts 211, 231 and 241 [Release Nos. 33-8350; 34-48960; FR-72] (December 29, 2003), and SEC Docket (1973-2004), 43 SEC-DOCKET 1330-129, Management's Discussion and Analysis of Financial Condition and Results of Operations; Certain Investment Company Disclosures, Securities and Exchange Commission, (May 18, 1989).

[16] "The Securities Laws and the Sustainability Accounting Standards Board" by Samuel P. Gunther, Richard H. Murray and Sheila A.S. Gunther, Bloomberg BNA Daily Environment Report (March 19, 2014).

[17] SASB, Insurance Companies and the SEC.

[18] Matrixx Initiatives, Inc. v. Sircusano, 131 S.Ct. 1309 (2011), available at http://www.supremecourt.gov/opinions/10pdf/09-1156.pdf.

is assessed by searching tens of thousands of source documents—including Form 10-Ks, shareholder resolutions, and SEC comment letters—for key words related to 43 general sustainability issues. This "heat map" provides initial indication of investor interest in certain issues. Evidence of financial impact is gathered by examining, among other things, sell-side research, investor call transcripts, third-party case studies, and news articles for evidence of impact on revenue, costs, assets, liabilities, and cost of capital. After identifying a minimum set of issues for an industry, for which there is solid evidence of both investor interest *and* financial impact, SASB identifies and documents existing metrics and practices used to account for performance on each issue. SASB standards are then refined through feedback received via balanced industry working groups, a 90-day public comment period, and review by an external, independent standards council composed of experts in standards development, securities law, environmental law, metrics, and accounting.

Corporate issuers and investor users are driving the creation and adoption of SASB standards. To date, more than 1,890 experts representing $21 trillion assets under management and $9.5 trillion market capital have participated in SASB's standards development process.

SASB has issued standards for 27 industries in four sectors, which constitutes 40 percent of SASB's planned work. SASB will issue standards for 80+ industries in 10 sectors by 2016.[19]

A natural progression

SASB is not calling for a new regulatory regime. Rather, SASB's objective is to improve the completeness of material information made available to investors via existing regulatory requirements and in compliance with U.S. securities law. Today, investors do not have all the information they need to determine how companies are adapting to a changing reality and to compare companies in the same industry with each other. SASB standards enable a natural progression in the evolution of the information available to the capital markets.

[19] Sustainability Accounting Standards Board website, available at http://www.sasb.org

Stanford SOCIAL INNOVATION Review
Informing and inspiring leaders of social change

Taking Impact Investing and Accounting Full Tilt
More foundations are deploying a full range of financial investment vehicles to yield positive social and financial returns, and using new tools to track impact data.
By Clara Miller & Jean Rogers
Jul. 18, 2014

Source: http://www.ssireview.org/blog/entry/taking_impact_investing_and_accounting_full_tilt *(Retrieved May 19, 2015)*

Foundations usually speak about innovation in terms of how they deliver program grants to nonprofits, where they fund, or how they measure results that would not have happened "but for" foundation dollars. But there's another way to look at philanthropic opportunity these days: Today's interconnected problems are stirring more foundations to invest *all* assets affirmatively to support their missions and align their holdings with their fiduciary duty to the public.

This requires taking a more active approach—learning what is in foundation portfolios and assessing how these holdings might support (or undermine) broader philanthropic goals. And while assessing and tracking the social performance of any company (nonprofit or for-profit) is challenging, regular, credible data on social performance (comprising social, environmental, and governance track records) are becoming more readily available.

While trying to account for positive and negative social impact of all investments is relatively new, the ideas and practice behind impact investing are not. Early on, Rockefeller, Carnegie, Ford, and others all made mission-aligned loans and equity investments in addition to grants.

But even now, when foundations make mission-aligned investments, they largely maintain the traditional bright line between the conventionally invested "endowment," (100 percent of assets, not aligned with mission) and the philanthropic side (5 percent of the endowment value, earned as income from the endowment, and disbursed annually in grants for mission).

Yet increasingly, stirred by the demands of urgent, outsized, and "wicked" problems that require muscle far beyond that provided by the traditional scope of grants or program-related investments alone, foundations are looking to do more. At the Heron Foundation, we are continuing our long-time dedication to this approach by increasing our mission-aligned investing from 40 percent to 100 percent of our assets—grants, loans, equity shares, everything.

As a recent *SSIR* blog post, "Mission-Driven Returns," points out, obstacles are numerous. They include regulatory complexity, a perceived risk-return mismatch, limited expertise among traditional investment advisors, difficulties measuring impact performance, and a circumscribed view of fiduciary responsibility. The authors also point out that timeworn habits have prevented foundations from widely embracing this approach.

But things are changing. Organizations are overcoming some of these barriers. In Heron's case, this has meant finding investment advisors with expertise that matches our investment appetite, revising our investment policy statement to emphasize the private foundation's fiduciary duty of obedience to mission (along with duties of care and loyalty), looking to achieve credible mission exposures across *all* asset classes, and combining our investment and grantmaking into one capital deployment unit to facilitate a

more active investing operation. As a result, we're de-emphasizing modern portfolio theory for a more bottom-up, and therefore more "asset aware," approach.

Most importantly, however, this approach means that we must collect data on the social and financial performance of *all* investments across the board (including grants and program-related investments) on an ongoing basis. The question has become, "What's the best use of a Heron dollar for mission and financial return, taken together?" No foundation's portfolio's performance is static. As a credible "all in" social investor, we need to track both, and track them over time.

For any foundation looking to—at the very least—eliminate mission-undermining positions from its portfolio, measuring mission performance with reliability and integrity, across the range of exposures in a portfolio, is paramount. One challenge has been a lack of comparable data on the sustainability (meaning environmental, social, and governance, or ESG) performance of public companies. But data providers, standard setters, and ratings providers are emerging. For example, the Global Reporting Initiative, the International Integrated Reporting Council, and the Carbon Disclosure Project have advanced standalone sustainability reports, integrated reports, and the disclosure of climate-related data (respectively). More and more organizations are contributing profile and attracting supporters to the emerging systems of performance measurement.

Recently, the Sustainability Accounting Standards Board (SASB) has focused on developing data standards for public companies to disclose material sustainability information in mandatory filings to the Securities and Exchange Commission, using a process of stakeholder involvement similar to that employed by the Financial Accounting Standards Board (FASB) for financial data and reporting. With SASB standards in place, investors will be able to type in a company ticker and pull up ESG data points—sustainability fundamentals alongside financial fundamentals—and benchmark the relative performance of companies on mission-related dimensions. SASB's Sustainability Industry Classification System (SICS) surfaces industries with the greatest potential for solving global sustainability challenges, allowing investors to allocate their portfolios accordingly.

Heron is far from alone in the quest for data. Other investors and data providers—including Bloomberg Philanthropies, The Generation Foundation, The Rockefeller Foundation, The Gordon and Betty Moore Foundation, and The Doris Duke Charitable Foundation—are funders of SASB and other data-oriented organizations. KL Felicitas, US Social Investment Foundation, and the G8 Social Impact Investment Task Force, to name just a few—are working to embed the principles of impact investing into the mainstream investment process by building a robust and independent data infrastructure. Impact investing principles are entering the DNA of the economy, and they will change the game for all.

It's not a moment too soon—like it or not, *all* investing is impact investing, and we need more enthusiasts. The real challenge is that many investors (including philanthropic investors such as foundations) are often unaware of the social performance of the companies they invest in. Many perform negatively on social criteria, sometimes in direct opposition to the missions of the foundations that own their shares or buy their debt, and may have more negative impact than grants have positive—or even, vice versa.

Business model and accounting innovations are not glamorous, and we don't often discuss them in the social sector. But new and better data entry/audit formats and tracking systems allow us to examine the true impact of our investment decisions, to create comparability in the larger market, and thus to push capital to seek the most broadly positive results for society—and avoid the negative ones.

Private foundations that invest on behalf of the public are running out of excuses. It's time for more of us to join the burgeoning group of investors who are making the financial investment needed to build a diverse data infrastructure, use it as customers, and as a result deploy a full range of financial investment vehicles to yield maximum positive social and financial performance for a world that is urgently in need.

FT FINANCIAL TIMES

Give Investors Access to All the Information They Need
By Michael Bloomberg and Mary Schapiro
May 20, 2014

Source: http://www.ft.com/cms/s/0/0d9ccea6-db66-11e3-94ad-00144feabdc0.html#axzz3ac7I9qtb
(Retrieved 5/19/15)

The most valuable currency in financial markets is reliable information. Without it, investors are unable to make informed decisions about where to allocate their capital, which hurts companies' ability to attract it and puts a drag on economic growth. Transparency is an economic engine.

For decades, investors' decisions have been aided principally by financial statements. But such information gives an incomplete picture of a company's health.

Many other factors affect the sustainability of a business, both internal (such as talent recruitment and retention) and external (such as constraints on natural resources). How effectively a company addresses such issues can profoundly affect its prospects. The trouble is, investors and shareholders often do not have ready access to comparable information about these issues.

A 2014 Ernst & Young study found that two-thirds of global investors evaluate non-financial disclosures. However, only half of this group uses a structured process to make their assessments. A way of providing standardised information to investors is required.

Take climate risk, for example, and consider two property development companies, both valued at $1bn. If one owns buildings that are in a coastal flood plain and the other does not, do you – as an investor – want to know?

Of course you do. But right now, such information it is generally not disclosed in financial filings. It may be difficult to find, evaluate and compare.

Similarly, investors want to know which automobile companies are making the most progress in developing alternative fuel vehicles; and which insurance companies have identified how much vulnerability their insured assets face as sea levels rise, storms intensify and business is interrupted. But, for the most part, investors do not know the answers to these questions.

In fact, sustainability issues that are not reflected on financial statements arise in every industry. Consider counterfeit drugs. The global market for counterfeits is estimated at $431bn – representing 1 per cent of US pharmaceutical supply, and 10 to 15 per cent of the world's pharmaceutical supply – which eats into corporate revenue and carries a deadly toll. Investors rightly want to know how this affects companies. But that information can be very hard to find.

The same is true for data security in the consumer finance industry. In 2012 global fraud losses for global credit and debit card companies amounted to $11.3bn. Which companies have been most successful at combating fraud? That information is difficult to obtain.

Lastly, look at hardware products that depend on minerals such as tantalum and tin, often derived from unstable regions where mining them can fuel conflict. Metals such as tantalum are crucial and scarce. Yet mobile phones containing them are discarded in landfill sites when they could have been recycled.

Although some companies share information on sustainability, reporting is not standardised and is usually geared toward advocacy groups rather than those with a financial interest. The time has come to give investors comparable, standardised data on these increasingly significant risks and opportunities.

Standardising disclosure of sustainability information could bring significant financial benefits for shareholders and potential investors – and help strengthen the long-term health of our global economy.

To accomplish this, an organisation founded in 2011 – the Sustainability Accounting Standards Board, for which we serve respectively as chair and vice-chair – is working with U.S.-listed corporations and investors to create industry-specific measurement and reporting standards around non-financial data. The standards are designed for use in the management discussion and analysis section of Securities and Exchange Commission filings.

Together with investors representing $17tn of assets under management and companies representing $8tn of market capital, we are identifying uniform metrics that will help investors compare companies within more than 80 industries in 10 sectors. In addition, the standards will help companies gauge their strengths, weaknesses and position relative to competitors.

To be clear: these standards are not an attempt to change any laws about what businesses must disclose. It remains up to each board to decide what information is material to their investors. Rather, our aim is to make disclosure more cost-effective for companies and more useful to their owners.

Adopting non-financial reporting standards will be an important step forward for transparency in our capital markets. It will help set our companies on a course for long-term growth.

In the process, it will also make our economy more resilient and competitive, protecting it against costly risks that – once they are known and properly valued – can be avoided.

The Great SASB

SASB is developing standards for disclosure of material environmental, social and governance issues not covered by the US SEC.

By Holly Clack and Andy Savitz

September 2013

Source: http://issuu.com/accaglobal_publications/docs/ab_int_sept13_comp_rgb_150 (Retrieved 9/16/13)

What would be the financial impact on a multinational drug company if one of its blockbuster drugs was counterfeited? How big an economic loss would be suffered by a commercial bank that found itself unable to attract the top-tier talent it needed to meet its growth targets? How will insurance company profits be affected if super storms become the norm?

If you answered 'I have no idea', you're not alone. Current accounting guidance and practice don't even attempt to quantify the material social, environmental and governance issues that most companies must deal with today. 'The relevance of accounting information in financial statements is decreasing at an alarming rate,' according to Baruch Lev, a finance and accounting professor at New York University's Stern School of Business.

Existing accounting standards were developed at a time when a company's growth and value depended almost exclusively upon its access to financial capital. Today the long-term performance and prospects of corporations also depend on social and environmental capital, and market values increasingly reflect these factors. As a result, triple bottom line (TBL) reporting is becoming a fact of life: such reporting increased from 20% to 53% by S&P 500 companies between 2011 and 2012, according to the Governance and Accountability Institute. But it is critical to move from reporting to valuation and to account for material sustainability-related issues, so that they can be included in a company's financial disclosures.

Enter SASB

The Sustainability Accounting Standards Board (SASB) was created two years ago based on the idea that financial reporting must reflect the reality of the TBL. SASB is developing accounting standards for disclosure of material environmental, social and governance issues that are not addressed or disclosed by companies under the existing rules and guidance in the US Securities and Exchange Commission's (SEC) Forms 10-K and 20-F.

Although SASB is not affiliated with the US Financial Accounting Standards Board, it hopes to attain a similar position in regard to non-financial issues to the one FASB has achieved for financial issues, requiring companies to provide a more complete picture to investors and other stakeholders.

Like F Scott Fitzgerald's Great Gatsby, the great SASB is nothing if not bold and full of hope. By 2015, SASB intends to create accounting standards for about 80 industries grouped into 10 sectors. SASB supporters believe that the time is right for this ambitious effort. The American National Standards Institute (ANSI) has accredited SASB to develop these standards, thereby ensuring that the SASB process will be 'balanced, accessible and responsive' and that all stakeholders will be heard 'without dominance by any party and in a manner that is open to public scrutiny'.

Like Gatsby, the great SASB has opened its doors to the world, and huge throngs have come to the party. It remains to be seen whether these celebrants are merely the young and careless or serious players that can make meaningful change happen. The evidence tends to suggest both. Although hundreds of business leaders have participated in the working groups, very few of them are senior and none of them are official representatives of their organisations. So it's impossible to predict whether their companies will ultimately support SASB's efforts. That said, the draft standards that have been developed thus far are thoughtful, rigorous, well researched and practical. They also address some of the biggest problems and opportunities facing the world.

To illustrate, the standards for the biotech and pharmaceutical industries, released 31 July, set forth a number of potentially material issues, including:

* pharmaceutical water contamination – an environmental risk;
* access to medicines – a social opportunity; and
* corruption and bribery – governance risks.

The guidelines explain each issue, provide evidence for its potential material impacts on companies and investors, and estimate the timing of the impacts. On counterfeit drugs, for example, the guidance states that 10% to 15% of the world's drug supply is counterfeit, causing 100,000 deaths annually. One illustrative case is counterfeit Avastin. Avastin is a cancer medication produced by Roche's Genentech division that typically sells for $2,400 per 400mg vial and generated $5.8bn in revenues in 2012. The impact of fake Avastin on Genentech includes reduced sales, potential liability and the loss of consumer confidence in the short and long term.

Other standards affecting companies in the finance, technology, communications, non-renewable resources and transportation sectors are already well advanced through SASB's pipeline. In 2014, SASB will convene working groups in services, resource transformation, consumption, and renewable resources and alternative energy. SASB is scheduled to wrap up with infrastructure in 2015.

Why is SASB important?

SASB standards will be a significant element of integrated reporting, through which all material information on a company will be disclosed in one place. If SASB succeeds, its standards will eventually be incorporated into SEC regulated disclosures.

Companies that are now reporting on the triple bottom line using the Global Reporting Initiative (GRI) or other sustainability reporting frameworks will need to measure, discuss and report on material TBL issues in their financial disclosures. Information that is not material to shareholders, but is of importance to other stakeholders, may be included elsewhere in the annual report, in a separate TBL reort, or on the company's website.

Although the SEC has asked to be briefed on SASB's progress on a quarterly basis, no commitment by the agency is expected before the completion of the standards in 2015. The green light is, if anything, further away than the one at Daisy's dock. SASB leadership is also meeting with the Public Company Accounting Oversight Board (PCAOB), established to ensure quality audits of public companies in an accounting industry that was previously self-regulated, because its main goal is the same as SASB's – investor protection.

What should you do now?

The great SASB may not achieve all its aspirations, but it should succeed in catalysing some important changes in accounting and disclosure rules, especially if environmental and social problems continue to dominate headlines and impede economic growth. Accountants and auditors will play an important role in the development, adoption and implementation of the sustainability accounting standards. Hopefully, the standards that emerge will be relevant and useful and will come with the technical guidance required to do the job. Accountants and auditors can:

* Learn more by participating in SASB's webinar series. Email: learn@sasb.org.
* Consider the kinds of material disclosures your company or clients will need to make under emerging SASB standards. Participate in an Industry Working Group, review the industry-specific standards as SASB issues them, provide feedback as appropriate or join SASB's pilot program commencing in 2014.
* Review SEC's Regulation S-K, Item 303 – Management's discussion and analysis (MD&A) of financial condition and results of operations, which requires disclosure of any known trend, demands, commitments, events or uncertainties that are reasonably likely to have a material effect on a company's operating results or financial condition. This may become the selected 'home' for reporting on sustainability accounting metrics and is a logical place to see any such disclosures today if corporations choose to make them.
* Review the American Institute for Certified Public Accountants (AICPA) AT Section 101 – Attest Engagements, which governs how an attest engagement should be performed, in the context of preparing for or conducting an audit of sustainability accounting metrics. Obtain specialised training, when it becomes available, in order to better prepare for or conduct audits of compliance with SASB standards.

Will the great SASB reach its ambitious goals? If F Scott Fitzgerald knows, he's not saying.

THE WALL STREET JOURNAL.

Pilot Program: Sustainability Reporting Guidelines

By Emily Chasan
July 31, 2013

Source: http://blogs.wsj.com/cfo/2013/07/31/pilot-program-sustainability-reporting-guidelines/ (Retrieved 7/2/2013)

The Sustainability Accounting Standards Board on Wednesday offered guidelines for the health-care industry to set consistent metrics for reporting environmental, social and governance data in their annual reports.

The standards, which are voluntary, will be tested over the next few years in a pilot program to see whether the costs of reporting such information matches the benefits, according to Dr. Jean Rogers, executive director and founder of the SASB, a nonprofit organization based in San Francisco.

The group targeted the health-care sector, which includes everything from biotechnology and pharmaceutical companies to managed-care providers, because it represents almost one-fifth of U.S. gross domestic product and is one of the biggest users of energy.

“Investors really need to be able to benchmark peer-to-peer performance and that’s what’s been missing from this whole sustainability conversation,” Ms. Rogers told CFO Journal.

The aim is to get companies to disclose specific metrics on issues including employee turnover, ethical marketing, energy usage, supply chain quality management, and pricing fairness. For example, one metric would encourage companies to disclose the ratio of their net price increases to the U.S. Consumer Price Index.

The U.S. Securities and Exchange Commission already requires public companies to disclose material risks in the management discussion and analysis section of annual reports, but the way those metrics are disclosed is entirely up to the company.

For example, last year, Bristol-Myers Squibb Co. warned in its annual report that counterfeit versions of its products could have a “negative impact” on its business and reputation. GlaxoSmithKline PLC also discussed counterfeit medicines in its annual 20-F report filed with the SEC, but was more specific, noting that in China it had added serial number to 31 products, resulting in a “significant” reduction of reports of counterfeit medicine.

“Different types of investors seek their own types of disclosures,” said Laura Francis, chief financial officer at Auxogyn Inc., a reproductive medical technology startup.

“For a company like ours sustainability is survival,” said Ms. Francis, who said she regularly discusses supply management issues with investors, “but life sciences investors often do think closely about a company’s mission.”

COMPLIANCE WEEK
THE LEADING INFORMATION SERVICE ON CORPORATE GOVERNANCE, RISK AND COMPLIANCE

Sustainability Reporting Gets Standard
By Jaclyn Jaeger
August 13, 2013

Source: http://www.complianceweek.com/pages/login.aspx?returl=/sustainability-reporting-gets-standard/article/306729/&pagetypeid=28&articleid=306729&accesslevel=2&expireddays=0&accessAndPrice=0 (Retrieved 9/12/13)

Some revolutionary changes are happening in the world of sustainability reporting that—for better or worse—demand the attention of companies.

The Sustainability Accounting Standards Board, a non-profit standard-setting body established in 2011, has issued its first set in a planned series of industry-specific reporting standards, designed to bring uniformity to how companies account for the environmental, social, and corporate governance risks that matter most to their operational and financial performance. First industry up at bat: healthcare. The inspiration for SASB and its standards sprung from investor activists clamoring in recent years for greater disclosure of "ESG" performance. Companies responded by publishing annual reports of their corporate social responsibility efforts, but a lack of standard disclosure metrics left investors unhappy since they couldn't compare one company's CSR efforts against another's. Enter SASB.

Accredited by the American National Standards Institute to set standards for disclosure of sustainability issues by U.S. publicly listed companies, SASB set out to identify material ESG issues and develop standardized performance metrics for 88 specific industries across 10 sectors. By following the same definition of materiality as defined by the Securities and Exchange Commission, the hope is that companies will use the ESG standards in their annual Form 10-K reports.


Rogers

Jean Rogers, founder and executive director of SASB, says the intent of the group is to become for ESG reporting what the Financial Accounting Standards Board has been for financial reporting. "Our goal is to standardize the disclosure of these material sustainability issues," she says.

The SEC requires public companies to disclose material information in the Management Discussion and Analysis section of their annual reports—but how ESG risks fit into the mix of material data has always been an elusive practice at best. For that reason, some sustainability executives say the standards are a welcome development.


Tew

"Until SASB came along, it's been extremely difficult to compare apples-to-apples," says Scott Tew, executive director for the Center for Energy Efficiency and Sustainability at Ingersoll-Rand. "The only way you can compare apples-to-apples is for everyone to agree on what is most material for a particular industry."

SASB developed its standards by establishing working groups for each industry composed of stakeholders, including companies, investors, analysts, auditors, and consultants.

Ingersoll-Rand is one of several companies that sit on SASB's advisory council. Other companies include Hershey Co., McDonald's, JP Morgan, Johnson & Johnson, UPS, Con Edison, and several more.

Rogers says that SASB has had “no problem getting companies to participate”—because of, rather than in spite of, ESG reporting fatigue. “They're tired of spending a lot of time and money doing so many different initiatives that aren't necessarily looked at by investors,” she says.

What's more, “investors tell us the same thing,” Rogers adds. “They're inundated with so much information that it makes it difficult for them to ascertain what's material. There is angst on both sides.”

Carrots and Sticks

For many other companies that may (quite understandably) groan over the idea of another ESG reporting initiative, be warned that investors and regulators alike are following these developments closely.


Nieland

“It's surprising how quickly SASB has established a level of prominence and impact in this space,” says Kathy Nieland, U.S. sustainable business solutions leader at PwC. “Investors are absolutely taking note of what standards they're developing.”

Even though the use of SASB-developed metrics in SEC reports is voluntary, SASB is hoping to change that. “It's really up to the SEC to enforce the inclusion of this information in the Form 10-K,” Rogers says.

Anne Sheehan, director of corporate governance at pension giant CalSTRS, which has more than $170 billion under management, says the SEC likely will be a “very active observer” in SASB's efforts, given that the agency's role is to ensure investors have material information. “I don't know in terms of formal rulemaking that the SEC is there yet.”


Aguilar

SASB briefs the SEC on its progress with quarterly updates and the evidence it gathers through research. Whether the SEC will actually enforce the standards on public companies is still an open question. Commissioner Luis Aguilar, for example, has long supported the idea of more disclosure about risks around climate change. On the other hand, the agency has a full plate struggling to implement rules for the Dodd-Frank Act.

“Whether or not they're successful will be the proof as to whether they're legitimate or not,” says Cary Krosinsky, executive director for the Network for Sustainable Financial Markets.


Krosinsky

The value proposition for companies is that the standards focus on issues that matter most to U.S. companies. In comparison, efforts such as the Global Reporting Initiative and the International Integrated Reporting Committee are guidelines focused on a global scale—and European views on CSR, for example, can be quite different from material disclosures under U.S. securities law.

At the very least, SASB's efforts have sparked some companies to think of sustainability practices in new and innovative ways. “Our strategy has been to integrate sustainability thinking into how the company operates its business,” Tew says. “We're really working on changing some of our already-existing processes.”

“Until recently we weren't formally asking our design engineers to think about the materials they choose for future products, or to evaluate what happens at the end of a product's lifecycle,” Tew says. “All that has changed now, because we've changed the process of how we develop products.”

What's Next

SASB issued its first set of standards on July 31, beginning with the healthcare sector and focusing on pharmaceuticals, biotechnology, medical equipment and supplies, healthcare delivery, healthcare distributors, and managed care.

For pharmaceutical companies, for example, SASB has developed standards on how to report on access to medicines, drug safety and side effects, safety of clinical trial participants, affordability and fair pricing, ethical marketing, counterfeit drugs, and efficiency in energy, water, and waste.

The standards were developed using a rigorous process that included industry working groups, a public comment period, and review by an independent standards council. The working groups for the healthcare sector, which included 127 survey responses, represented publicly traded companies with more than $800 billion in market capital and investment firms with more than $952 billion in assets under management.

SASB plans to release standards for the financial sector this fall, followed by technology and communications. Standards for the non-renewables sector are also in development.

As with any new undertaking, kinks will need to be kneaded out along the way, Sheehan says. “It's going to be an ongoing, iterative educational process to perfect this effort as they address various industry sectors.”

“The only burden is that it takes a long time to get it right,” Tew says. “It's time consuming. It's intense. It's detailed, but it's also being done right.”

Sustainability Accounting Standards Board
75 Broadway
Suite 202
San Francisco, CA 94111
415 830-9220
sasb.org

Media Contact:
Amanda Medress
Associate Director, Communications
Amanda.Medress@sasb.org
(415) 830-9220 ext. 106