Jeffrey Hales: SASB Standards Council Chairman

- Catherine W. and Edwin A. Wahlen, Jr. Professor of Accounting at the Georgia Institute of Technology – Ernest Scheller Jr. College of Business
- Research focuses on accounting standard setting and regulation, individual decision making, and behavioral finance
- Editor for Accounting Horizons and an ad hoc editor for Contemporary Accounting Research and European Accounting Review
- Former Research Fellow at the Financial Accounting Standards Board (FASB)
- Serves on FASB's Financial Accounting Standards Advisory Council and chairs the Standards Council for the Sustainability Accounting Standards Board.
The positions conveyed here are my own opinion and do not necessarily represent the opinions of SASB board and/or staff members. Official positions of SASB are arrived at only after due process.
The SASB Mission
Improved sustainability disclosure enhances market efficiency

SASB’s mission is to develop and disseminate sustainability accounting standards that help companies disclose material, decision-useful information to investors in a cost-effective way.

That mission is accomplished through a rigorous, transparent process that includes evidence-based research and broad, balanced stakeholder participation.

Facts about SASB
- Independent 501(c)(3) non-profit
- Incorporated in 2011
- Develops standards for 79 industries in 10 sectors for use in mandatory filings such as the Form 10-K and 20-F
Strong Support for SASB Vision

SASB’s Board is informed by experience, character, and commitment

Michael R. Bloomberg – Chair
Philanthropist, Founder of Bloomberg LP, and the 108th Mayor of New York City

Mary Schapiro – Vice Chair
Promontory Advisory Board Vice Chair
Former Chairman – SEC

Alan Beller
Senior Counsel – Cleary Gottlieb Steen & Hamilton

Audrey Choi
CEO – Institute for Sustainable Investing, Morgan Stanley

Jack Ehnes
CEO – CalSTRS

Steven O. Gunders, CPA
Partner – Deloitte & Touche LLP (Retired)

Dan Hanson, CFA
Partner & Co-Chair, Investment Strategy Committee – Jarislowsky Fraser Global Investment Management

Robert H. Herz
Former Chairman – FASB

Erika Karp
CEO – Cornerstone Capital Inc.

Shawn Lytle
President – Delaware Management Holdings, Inc.

Ken Mehlman
Member & Global Head of Public Affairs – KKR

Clara Miller
President – The F.B. Heron Foundation

Catherine Odelbo
Executive Vice President, Corporate Strategy and Partnerships – Morningstar Inc.

Kevin Parker
CEO – Sustainable Insight Capital Management

Aulana Peters, JD
Former Commissioner – SEC

Arnie Pinkston, JD
General Counsel, Allergan (Retired)

Curtis Ravenel
Global Head, Sustainable Business and Finance – Bloomberg LP

Jean Rogers, PhD, PE
Chief Executive Officer & Founder – SASB (Ex-officio)

Laura Tyson, PhD
Director, Institute for Business and Social Impact – Berkeley Haas School of Business

Elisse Walter, JD
Former Chairman – SEC

Edward D. White, JD
Managing Partner – Fahr LLC
### Organizational Milestones

- Jean Rogers founded SASB and started as CEO
- SASB incorporated in California as 501(c)(3) nonprofit
- Board of Directors formed, Bob Eccles named as inaugural chair
- Harvard IR paper, “From Transparency to Performance,” authored by Steve Lydenberg, Jean Rogers, David Wood
- First operating grant received from Bloomberg Philanthropies
- SASB’s public launch of standards-setting activities
- Jeff Hales appointed as chair of Standards Council
- Accreditation received from the American National Standards Institute (ANSI)
- Release of Conceptual Framework
- Industry working group participants reach 1,000 (1/3 corporate professionals, 1/3 investors, 1/3 other stakeholders)
- Michael Bloomberg and Mary Schapiro appointed as Chair and Vice Chair of Board of Directors
- Harvard Business School published case on SASB
- Partnership program for software providers launched
- Robert Herz, former head of FASB, appointed to SASB Board of Directors
- Standards Navigator, a digital tool to access the Standards, launched
- Industry Working Group participants exceed 2,000
- Data Provider Partner Program launched to give investors access to high-quality sustainability information
- Fundamentals of Sustainability Accounting (FSA) Credential launched
- Implementation Guide for Companies released, providing guidance for issuers
- Industry Working Group participants exceed 2,800

### Provisional Standards Issued

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<td>7 industries in Financials sector</td>
<td>5 industries in Resource Transformation sector</td>
<td>8 industries in Infrastructure sector</td>
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<td>6 industries in Technology &amp; Communication sector</td>
<td>5 industries in Consumption sector</td>
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A Growing Demand for Effective Disclosure
Global megatrends, economic evolution create challenges for companies, investors

REGULATORY PRESSURE
- Mandates in multiple markets (E.U., China, India, etc.)
- Exchange listing requirements and guidance
- Financial Stability Board (FSB) Task Force on Climate Risk
- Regulation S-K Compliance

ECONOMIC PRESSURE
- Resource constraints and volatility
- Financial impacts of climate related risk
- Changing valuations and the rise of intangibles
- Transition to low carbon economy

INVESTOR PRESSURE
- Shareholder resolutions
- Questionnaire fatigue
- Calls for divestment
- Increasing engagement

STATE OF DISCLOSURE
- Proliferation of boilerplate disclosures
- Inability to discern material information or benchmark
- Inconsistent quality of data
- Inappropriate use of “materiality” in corporate communications
The SASB Difference
SASB standards are built around core principles

- Material Factors
- Industry-Specific
- Decision-Useful
- Cost-Effective
- Evidence-Based
- Market-Informed
“It is not sufficient that information merely be useful. Nor is it sufficient that only some investors might find a bit of the information to be important. Rather…the question of materiality ‘is universally agreed as an objective one, involving the significance of an omitted or misrepresented fact to a reasonable investor.’ Thus, materiality is an objective legal standard, not a subjective political one.”
Complementary Efforts

Mandatory and voluntary reporting serve different purposes for different audiences.

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

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

Alignment is key
(e.g., consistent use of the description “material”)

Stakeholders

Investors
Other Reporting Models – GRI

- **Link A**: US GAAP or IFRS
- **Link B**: G4 Sustainability Reporting Standards
Other Reporting Models – CDP

- Investors
- Reports and Analyses
- Survey Responses
- Corporations
- Surveys
- Signatories
Integrated reporting without additional regulation or reporting mechanisms

US GAAP governs presentation of the financials

True and fair representation of performance on material factors

Accounting Metrics integrate into MD&A, risk factors, and other sections as appropriate

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

Materiality in Practice as a Basis for Standards Setting
SASB standards include issues with demonstrated evidence of impacts on the financial condition and operating performance of a company.

Types of Financial Drivers
- Demand for Core Products and Services
- Market Share and Long-Term Growth
- Operational Efficiency/Cost Structure
- Governance, Volatility and Risk Factors
- Tangible and Intangible Assets and Liabilities

Disclosure Topics Examples
- Drug safety and side effects
- License to Operate
- Energy-efficient chemicals production
- Operational safety of gas pipelines
- Stranded coal assets

Financial Impact
- REVENUE
- COST
- COST OF CAPITAL
- ASSETS & LIABILITIES

Examples
- Demand for Core Products and Services
- Market Share and Long-Term Growth
- Operational Efficiency/Cost Structure
- Governance, Volatility and Risk Factors
- Tangible and Intangible Assets and Liabilities
Current State of Disclosure in the 10-K on SASB topics
Reporting lacks consistency, comparability, industry-specificity

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<td>Health Care Sector (58 companies)</td>
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75% of SASB disclosure topics are *already being disclosed in the 10-K—but not effectively*
Materiality Approach Validated by External Research
Harvard research correlates sustainability and financial performance

“Corporate Sustainability: First Evidence on Materiality,”
Working Paper by Mozaffar Khan, George Serafeim, and Aaron Yoon
Harvard Business School, 2015

Findings:

- Using SASB’s framework, Harvard researchers found that firms with good performance on ‘material sustainability issues’ and concurrently poor performance on ‘immaterial sustainability issues’ enjoy the strongest financial returns.

- They also found that 80 percent of corporate disclosures on sustainability are immaterial, having no correlation to financial performance.
“SASB’s standards support the SEC’s mission to protect investors and maintain efficient markets. In today’s world, where intangible assets comprise a significant portion of S&P market value, investors need industry-specific data on non-financial factors which are important to risk mitigation and long-term value creation.”

Aulana Peters
Former SEC Commissioner
### Sustainable Industry Classification System Underpins SASB

SICS™ industries are grouped by resource intensity and sustainability impacts

<table>
<thead>
<tr>
<th>Health Care</th>
<th>Non-Renewable Resources</th>
<th>Resource Transformation</th>
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<tbody>
<tr>
<td>Biotechnology</td>
<td>Oil &amp; Gas – Exploration &amp; Production</td>
<td>Chemicals</td>
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<td>Pharmaceuticals</td>
<td>Oil &amp; Gas – Midstream</td>
<td>Aerospace &amp; Defense</td>
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<tr>
<td>Medical Equipment &amp; Supplies</td>
<td>Oil &amp; Gas – Refining &amp; Marketing</td>
<td>Electrical &amp; Electronic Equipment</td>
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<td>Health Care Delivery</td>
<td>Oil &amp; Gas – Services</td>
<td>Industrial Machinery &amp; Goods</td>
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<td>Health Care Distributors</td>
<td>Coal Operations</td>
<td>Containers &amp; Packaging</td>
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<td>Managed Care</td>
<td>Iron &amp; Steel Producers</td>
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<td>Metals &amp; Mining</td>
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<td>Construction Materials</td>
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<th>Technology &amp; Communications</th>
<th>Infrastructure</th>
<th>Financials</th>
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<tbody>
<tr>
<td>Electronic Manufacturing Services &amp;</td>
<td>Electric Utilities</td>
<td>Commercial Banks</td>
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<td>Original Design Manufacturing</td>
<td>Gas Utilities</td>
<td>Investment Banking &amp; Brokerage</td>
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<td>Software &amp; IT Services</td>
<td>Water Utilities</td>
<td>Asset Management &amp; Custody Activities</td>
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<td>Hardware</td>
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<td>Consumer Finance</td>
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<td>Semiconductors</td>
<td>Engineering &amp; Construction Services</td>
<td>Mortgage Finance</td>
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<td>Telecommunications</td>
<td>Home Builders</td>
<td>Security &amp; Commodity Exchanges</td>
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<td>Internet Media &amp; Services</td>
<td>Real Estate Owners, Developers &amp; Investment Trusts</td>
<td>Insurance</td>
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<td>Real Estate Services</td>
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<tr>
<th>Renewable Resources &amp; Alternative Energy</th>
<th>Services</th>
<th>Consumption</th>
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<tr>
<td>Biofuels</td>
<td>Education</td>
<td>Agricultural Products</td>
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<td>Solar Energy</td>
<td>Professional Services</td>
<td>Meat, Poultry &amp; Dairy</td>
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<td>Wind Energy</td>
<td>Hotels &amp; Lodging</td>
<td>Processed Foods</td>
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<tr>
<td>Fuel Cells &amp; Industrial Batteries</td>
<td>Casinos &amp; Gaming</td>
<td>Non-Alcoholic Beverages</td>
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<td>Forestry &amp; Paper</td>
<td>Restaurants</td>
<td>Alcoholic Beverages</td>
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<td>Leisure Facilities</td>
<td>Tobacco</td>
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<td>Cruise Lines</td>
<td>Household &amp; Personal Products</td>
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<td>Advertising &amp; Marketing</td>
<td>Multiline and Specialty Retailers &amp; Distributors</td>
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<td>Media Production &amp; Distribution</td>
<td>Food Retailers &amp; Distributors</td>
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<td>Cable &amp; Satellite</td>
<td>Drug Retailers &amp; Convenience Stores</td>
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<td>E-Commerce</td>
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<td>Apparel, Accessories &amp; Footwear</td>
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<td>Building Products &amp; Furnishings</td>
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<td>Appliance Manufacturing</td>
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<td>Toys &amp; Sporting Goods</td>
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<th>Transportation</th>
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<td>Automobiles</td>
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<td>Auto Parts</td>
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<td>Car Rental &amp; Leasing</td>
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<td>Airlines</td>
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<td>Air Freight &amp; Logistics</td>
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<td>Marine Transportation</td>
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<td>Rail Transportation</td>
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<td>Road Transportation</td>
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Evaluation of the Materiality of Sustainability Issues in Each Industry

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

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

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

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

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

**Leadership and governance**
- Systemic risk management
- Accident and safety management
- Business ethics and transparency of payments
- Competitive behavior
- Regulatory capture and political influence
- Materials sourcing
- Supply chain management
A Rigorous, Transparent Process has led to Provisional Standards

SASB has entered a phase of deep consultation, analytics, field testing, and cost benefit analysis prior to codification of the standards for 79 industries.

The public comment period for the Conceptual Framework and Rules of Procedure governing the Codification Phase was completed on July 6, 2016.
# SASB Materiality Map

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

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**SASB Materiality Map™**

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

## ISSUES

<table>
<thead>
<tr>
<th>Environment</th>
<th>Health Care</th>
<th>Financials</th>
<th>Technology and Communications</th>
<th>Non-Renewable Resources</th>
<th>Transportation</th>
<th>Services</th>
<th>Resource Transformation</th>
<th>Consumption</th>
<th>Renewable Resources &amp; Alternative Energy</th>
<th>Infrastructure</th>
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### Improving Disclosure Effectiveness

**Moving from boilerplate to decision-useful disclosure**

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<th>BOILERPLATE</th>
<th>COMPANY SPECIFIC</th>
<th>SASB METRIC(S)</th>
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| **Cruise Lines Industry — Fuel Use & Air Emissions** | “We are subject to complex laws and regulations, including environmental laws and regulations, which could adversely affect our operations and any changes in the current laws and regulations could lead to increased costs or decreased revenue.” | “We measure our ability to use direct energy efficiently by calculating the amount of primary source energy we consume. **We have achieved a 21% cumulative reduction in unit fuel consumption since 2007** and look to further manage and reduce our fuel consumption costs in the future.” | ▪ Gross global Scope 1 emissions (CO₂-e)  
▪ Total energy consumed (GJ), percentage from heavy fuel oil (%), percentage from onshore power supply (OPS) (%), percentage from renewables (%)  
▪ Air emissions for the following pollutants: NOx, SOx, and particulate matter (PM) (t)  
▪ Average Energy Efficiency Design Index (EEDI) for new ships |
| **Auto Parts Industry — Energy Management** | “Higher raw material and energy costs around the world may offset our efforts to reduce our cost structure. As a result, higher raw material and energy costs could result in declining margins and operating results and adversely affect our financial condition.” | “We have launched several energy saving programs. **Our total energy consumption corresponds to 257,000 metric tons of CO₂ (using the Greenhouse Gas Protocol), which was an increase of 4% from 2012.** This is mainly a consequence of expanding production in China, which is dominated by coal based energy.” | ▪ Total energy consumed (GJ), percentage grid electricity (%), percentage renewable (%) |

Disclosure examples from FY 2013 annual SEC filings
“The more complete and reliable the information that investors have, the better markets work – and that benefits not only individual investors but all of society.”

Michael Bloomberg
Founder and CEO of Bloomberg LP; Chair of SASB Board of Directors
Integrated Into Investment Decisions
SASB standards and related products support a variety of investment strategies

MACRO TRENDS

- Which industries are facing the greatest sustainability headwinds?
- How do sustainability issues impact core industry drivers, such as consumer preference or regulatory change?

PORTFOLIO ALLOCATION

- How can I measure and diversify concentrated sustainability risk?
- What is sustainability’s impact on portfolio performance?

COMPANY BENCHMARKING

- Which companies are leaders?
- Which are laggards?

SECURITY VALUATION

- How should I adjust my discounted-cash-flow analysis or valuation metrics for sustainability risks and impacts?
Complete, Reliable Data Sets are Essential for Investor Use
SASB standards enable peer-to-peer comparisons and industry benchmarking
Robust Standards Designed to Yield Decision-Useful Information
SASB standards contain industry-specific disclosure topics, metrics, and guidance.

Table 1. Material Sustainability Topics & Accounting Metrics

<table>
<thead>
<tr>
<th>TOPIC</th>
<th>ACCOUNTING METRIC</th>
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<tbody>
<tr>
<td>Greenhouse Gas Emissions</td>
<td>Gross global Scope 1 emissions, percentage covered under a regulatory program, percentage by hydrocarbon resource</td>
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<tr>
<td>Air Quality</td>
<td>Air emissions for the following pollutants: NOx (excluding N2O), SOx, volatile organic compounds (VOCs), and particulate matter (PM)</td>
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<tr>
<td>Water Management</td>
<td>Total fresh water withdrawn, percentage recycled, percentage in regions with High or Extremely High Baseline Water Stress</td>
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</table>

Accounting metrics for each disclosure topic

Technical protocol for compiling data; activity metrics for normalization
A True and Fair Representation of Performance?
Voluntary sustainability reports are not decision-useful for investors

A 2013 study in Accounting, Auditing & Accountability Journal examined 23 GRI reports in energy and mining and found that, while ALL were rated by GRI as A or A+, 90 percent of the significant negative corporate (social or environmental) events identified in the news were “either omitted...or addressed in a...non-transparent fashion.”
“A thorough and robust due process is the most important asset of any standards-setting organization.”

Robert Herz
Former FASB Chair
Shaped By Market Consensus
SASB topics must achieve a high level of consensus among issuers and investors

Stakeholder-specific feedback on likely materiality of all proposed disclosure topics
(% of respondents, by interest group, who think suggested topics are likely to constitute material information)
On a recent webcast of FEI members, 48% of the participants polled stated that they were beginning to evaluate SASB disclosures for integration into their next 10-K filing.
SASB RULES OF PROCEDURE
Describes the processes, practices, and procedures that SASB follows to develop material, decision-useful, cost-effective sustainability accounting standards.
Proposed Rules of Procedure
Processes, practices, and procedures for standards development

- Establishes the **SASB Standards Council**, an independent, 9 member voting body to approve SASB standards and any subsequent changes.

- Establishes Board-level **Standards Oversight Committee** to enforce due process and administer complaints and appeals.

- Initiates process of “**Agenda Setting**” for ongoing maintenance of standards.

- Finished public comment period on **July 6th, 2016**.
SASB is in Deep Consultation on the Provisional Standards
For next 12-18 months, SASB will seek feedback on materiality and cost-effectiveness

“NAREIT generally supports development of standards for reporting issues that are material to investors in our industry. … We are also supportive of the emergence of standardized metrics. … [T]he overall benefits of having a standardized method to report material issues to investors could be substantial and could serve as a roadmap for companies to disclose this information in their required company financial reports.”

— Public comment letter from National Association of Real Estate Investment Trusts (NAREIT)

January 5, 2016

By end Q2 of 2016, SASB had responded to 100% of public comment letters.
“Today, investors make their decisions based on an array of information, which goes beyond mere profit and loss. Many believe that the era of sustainability or impact investing has arrived. Sustainability disclosure differentiates companies and it may foster investor confidence, trust, and employee loyalty. More importantly for investors, companies that adopt certain environmental, social, and corporate governance or ESG measures may perform better than those that do not.”
Regulation S-K Concept Release
Requested comments on disclosure of public policy and sustainability matters

Section F; pages 204-215

- What ESG issues are important to investment decisions?
- What would an ESG disclosure framework look like? Could it be flexible enough to address evolving issues?
- Would line-item disclosure requirements be consistent with The Commission’s rule-making authority? Would they yield immaterial information?
- Does information on ESG factors reported outside Commission filings address investor needs?

Responses were due July 21, 2016
Regulation S-K Concept Release
Provided opportunity for SASB to communicate key points to the Commission

- Investor demand for material sustainability information
- Corporate cost burden of CSR reports, questionnaires and shareholder resolutions
- Biased disclosure (i.e. “cherry picking”) in voluntary sustainability reports
- Proliferation of boilerplate information on material factors in mandatory filings
- Inability to distinguish immaterial from material information; unreliable data
- Selective disclosure of material information through questionnaires
- The need for investors to purchase ESG information from commercial services
- Inability of regulators to enforce disclosure against a market standard

A market standard on ESG disclosure is needed to meet investor needs, guide companies on materiality, and serve as the basis for compliance with Regulation S-K.
“Accounting standards are a key foundational element to our proposed ESG strategy going forward over next five years...we believe, at this point in time, it’s crucial for development of accounting standards for material ESG issues. SASB is a very important part of that solution.”

Ted Eliopoulos
CIO, CalPERS