

# Disclosure & Transparency Impact on Industry

Aspen Global Change Institute

W. Sisson

November, 2018

# Abstract

Are Forces Shifting Industry Towards Increased Environment and Social Responsibility?

# Economics: Invisible Hand to Eco Footprint



# Rachel Carson – CBS Reports





# Historical Context

1960's/70's – “Conscious Choices” to Act

EPA (Kennedy, Nixon)

Greenpeace, WWF

1980's – Increasing Awareness & Public Outrage

Visual (UCC – Bhopal; 3 Mile Island, Chernobyl; Exxon Valdez, ...)

Corporate Regulatory Impact and Enforcement

1990's – Business is Responding

Rio Earth Summit, Kyoto, WBCSD

2000's – Sustainability Reporting, Transparency

2010's – COP21, Sustainable Development Goals, ESG



# Regulatory Intervention

## Environmental Protection Acts

US Clean Air/Water Act (60's & 70's)

CAA for "Acid Rain" (SO<sub>2</sub> & NO<sub>x</sub>) (90's GHW Bush)

EU (1990's)



## "Erin Brockovich"

Environmental Litigation (CR<sup>+</sup>6)

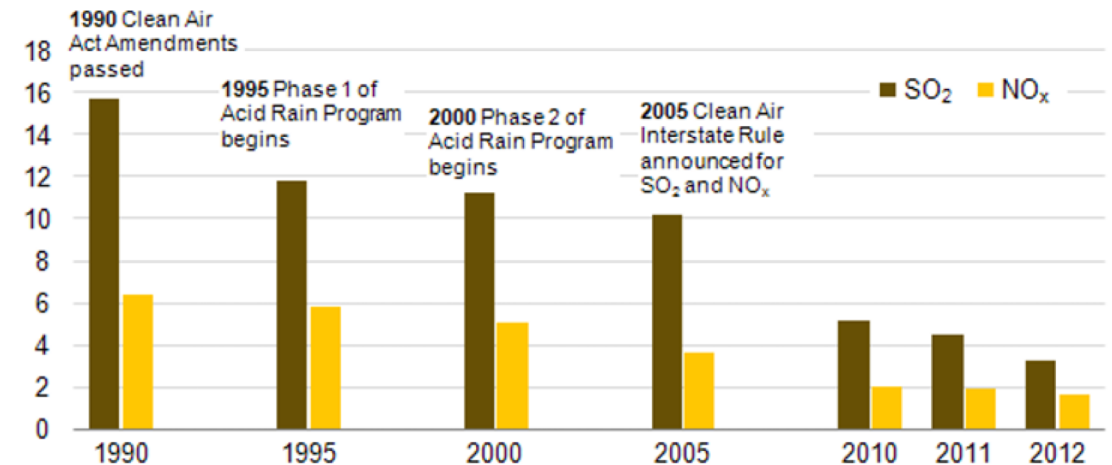
## Chemical Regulations

Kyoto, Montreal Protocol, Kigali

TSCA(US), REACH (EU++), RoHS, ...

UNFCCC/COP21 Paris Agreement

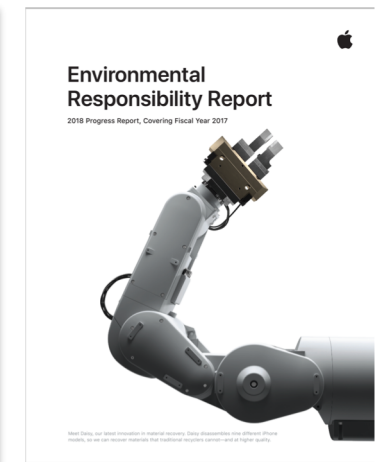
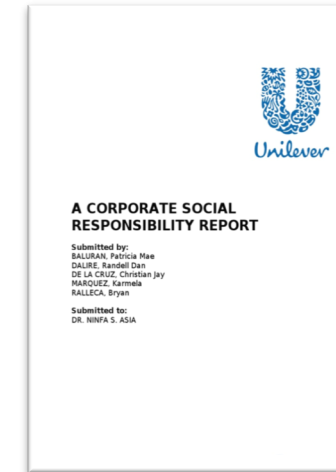
SO<sub>2</sub> and NO<sub>x</sub> emissions from the electric power sector  
million short tons



# Industrial Sustainability



Source: *Why Sustainability Is Now the Key Driver of Innovation*; Ram Nidumolu, C.K. Prahalad, and M.R. Rangaswami; HBR September 2009.



# Corporate Responsibility

“SP” Relationship

CSR Reporting

CDP: 7000 Companies (2017)

Positioning Leadership

Unilever’s Polman

J&J’s Earthwards®

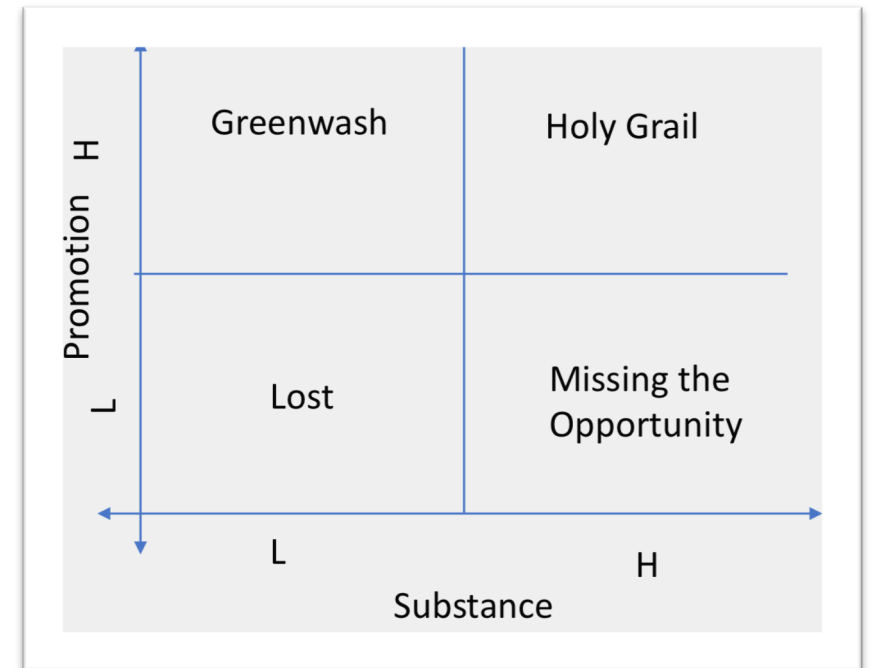
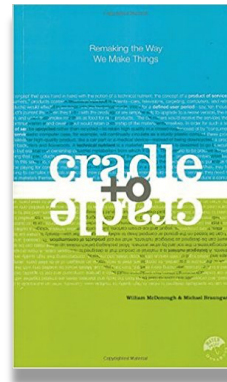
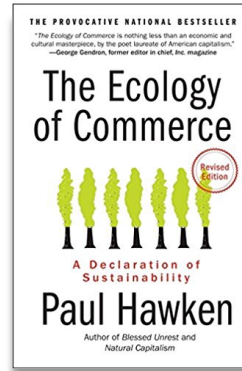
GE’s Eco-Magination™

Greening the Supply Chain

Circular Economy

Business Opportunities

Emerging: ESG and Risk



# Industry ESG Risk Context

*Entities, including businesses, governments and non-profits, face an evolving landscape of environmental, social and governance (ESG)-related risks that can impact their profitability, success and even survival.*

**Table 1: Definitions of ESG**

|               | MSCI definition                                                                        | Robeco definition                                                                                                                                                                                                                                                                                                             |
|---------------|----------------------------------------------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Environmental | Climate change, natural resources, pollution and waste and environmental opportunities | The contribution an entity makes to climate change through greenhouse gas emissions, along with waste management and energy efficiency. Given renewed efforts to combat global warming, cutting emissions and decarbonizing have become more important.                                                                       |
| Social        | Human capital, product liability, stakeholder opposition and social opportunities      | Human rights, labor standards in the supply chain, any exposure to illegal child labor and more routine issues such as adherence to workplace health and safety. A social score also rises if a company is well integrated with its local community and therefore has a “social license” to operate with consent.             |
| Governance    | Corporate governance and corporate behavior                                            | A set of rules or principles defining rights, responsibilities and expectations between different stakeholders in the governance of corporations. A well-defined corporate governance system can be used to balance or align interests between stakeholders and can work as a tool to support a company’s long-term strategy. |

*Enterprise Risk Management, Applying enterprise risk management to environmental, social and governance-related risks, COSO and WBCSD, October 2018*

## Environmental

What steps is the company taking to insure regulatory environmental compliance?

How has the company positioned itself for climate risks and resilience?

## Social

What is the company doing to promote worker health and safety?

Policies around conflict minerals and labor laws?

Societal role? Military business and weaponry?

## Governance

Policy, goals, and performance

Board level ownership and flow-down?

Transparency, public reporting, and assurance?



# ESG and Business Risk

“ **Environmental, social, and governance (ESG) factors relevant to a company's business can provide essential insights into management effectiveness and thus a company's long-term prospects.** ”

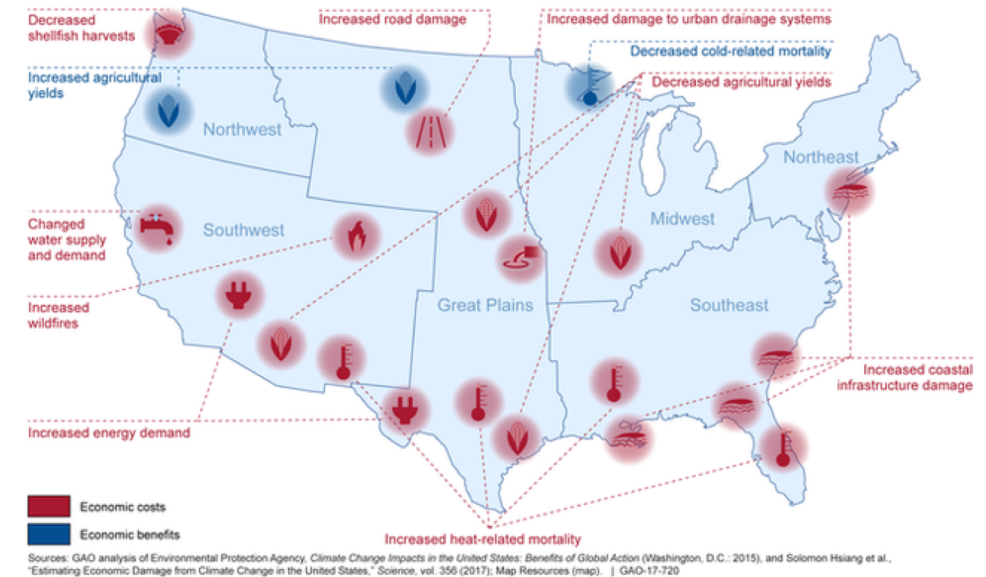


- Larry Fink  
Chairman and CEO, BlackRock

**Table 2.4: Top ten global business risks for 2018**

| Megatrend                                              | Description                                                                                                                            |
|--------------------------------------------------------|----------------------------------------------------------------------------------------------------------------------------------------|
| <b>Business interruption</b>                           | Supply chain disruption, factory fires, destroyed shipping containers, cyber incidents                                                 |
| <b>Cyber incidents</b>                                 | New threats such as “cyber hurricanes” and tougher data regulation; a single cyber attack can potentially impact hundreds of companies |
| <b>Natural catastrophes</b>                            | Numerous natural catastrophes in 2017 could indicate increases in the future due to the impact of a changing climate                   |
| <b>Market developments</b>                             | Waves of M&A activity, digital revolution, political uncertainty                                                                       |
| <b>Changes in legislation</b>                          | Changes in global trade agreements, uneven monetary and regulatory conditions between regions                                          |
| <b>Fire/explosion</b>                                  | Physical damage and business disruption result in losses from fire and explosions                                                      |
| <b>New technologies</b>                                | Technological advances, digitalization, interconnectivity and information exchange                                                     |
| <b>Loss of reputation/brand value</b>                  | Health and safety incidents, product recalls and data security breaches – exacerbated by social media and interconnected supply chain  |
| <b>Political risks and violence</b>                    | Terrorism, threats to transportation infrastructure and locations with large groups of people, increased political activism            |
| <b>Climate change/increasing volatility of weather</b> | Increasing frequency and severity of weather events                                                                                    |

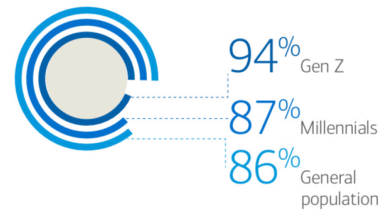
Adapted from 2018 Allianz Risk Barometer



Enterprise Risk Management, Applying enterprise risk management to environmental, social and governance-related risks, COSO and WBCSD, October 2018

# ESG & Industry's Stakeholders

Investors  
Suppliers  
Customers  
Employees  
Insurance  
Banking  
Gov't  
NGO's



Most consumers believe that companies should address ESG issues

ESG: Impact on Companies Doing Business in America and Why They Must Care; Bank of America/Merrill Lynch, 2018



We Are Still In declaration in June 2017

**Table 5.2: External stakeholder groups, information and communication**

| Stakeholder group                                                                                                          | Example information needs                                                                                                                                                                                                                                                                                                                              | Example communication methods                                                                                                                                                                                                                                                         |
|----------------------------------------------------------------------------------------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <b>Investors</b><br>Provide capital to the entity with an expectation of financial returns                                 | <ul style="list-style-type: none"> <li>Entity's approach for managing significant changes to the internal and external environment leading to ESG-related impacts or dependencies</li> <li>Understanding of how the entity identifies, assesses and manages its ESG-related risks (e.g., climate-related risks)<sup>6</sup></li> </ul>                 | <ul style="list-style-type: none"> <li>Annual general meeting of shareholders</li> <li>Annual report, risk filing or 10-K</li> <li>Integrated report</li> <li>Proxy</li> </ul>                                                                                                        |
| <b>Suppliers</b><br>Supply goods or services to the entity                                                                 | <ul style="list-style-type: none"> <li>Entity's standards for suppliers which may include areas such as ethics, integrity, legal standards, compliance, health and safety and environment</li> <li>Supplier performance against the entity's ESG-related standards</li> </ul>                                                                          | <ul style="list-style-type: none"> <li>Supplier code of conduct</li> <li>Report card, including, for example, quality, delivery, quantity delivered, performance history, incident report and comments</li> <li>Management meetings<sup>7</sup></li> </ul>                            |
| <b>Customers</b><br>Purchases the entity's goods or services                                                               | <ul style="list-style-type: none"> <li>Information on how the product was made (e.g., ingredients, country of origin, factory information)</li> <li>Information on how to use the product and whether it may impact the consumer's health and safety (e.g., side effects of pharmaceuticals)</li> </ul>                                                | <ul style="list-style-type: none"> <li>Responsible marketing practices (e.g., promoting accurate facts about the product)</li> <li>Product labeling (e.g., nutrition facts)</li> <li>Licensed, certified or authorized retailers (e.g., pharmacists)</li> <li>Focus groups</li> </ul> |
| <b>NGOs and communities</b><br>Hold entities accountable for impacts on their interest groups (e.g., environment, society) | <ul style="list-style-type: none"> <li>Entity's approach for mitigating against negative impacts to NGO interests (e.g., deforestation from palm oil extraction)</li> <li>Understanding of how the entity benefits the local and global environment and society (e.g., volunteer hours, employee monetary contributions to cancer research)</li> </ul> | <ul style="list-style-type: none"> <li>Annual general meeting of shareholders</li> <li>Integrated report</li> <li>Sustainability report</li> <li>Website</li> <li>One-on-one engagement or facilitated stakeholder meetings</li> </ul>                                                |

Enterprise Risk Management, Applying enterprise risk management to environmental, social and governance-related risks, COSO and WBCSD, October 2018

# ESG and The Next Decade

## Increasing Transparency and ERM

Consolidation/Standardization (SASB)

MNC to SME;

EU Directive on Non-Financial Reporting; TCFD

## Disclosure Labeling: e.g. Real-Estate

Voluntary to Investment Grade: LEED to performance standards (EPBD)

Public information

## Sustainable Living Standards

Sub-National Performance

Ratings (LEED) for Cities

## Government

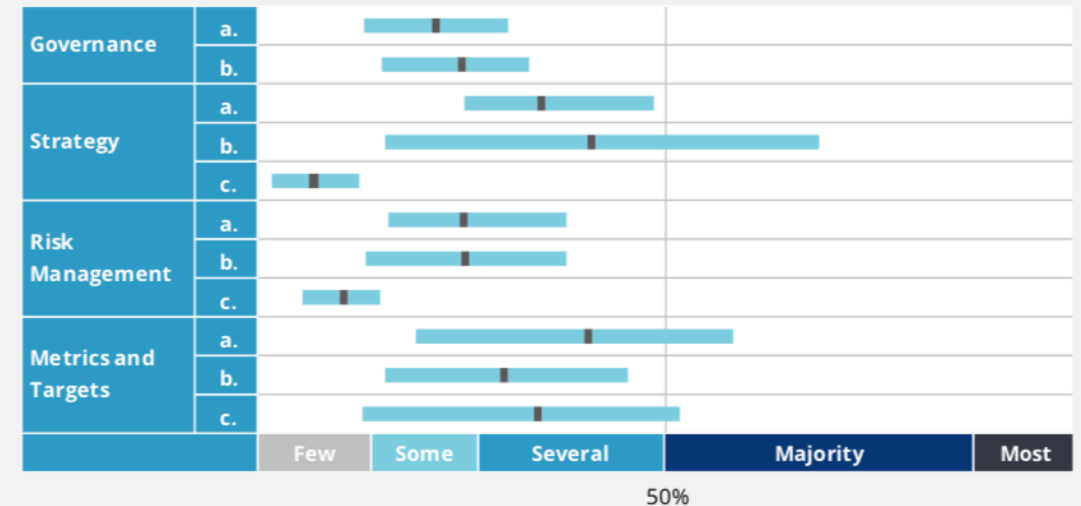
Price Signals (Carbon, Water)

SDGs, Climate and Resiliency Policy/Regulation

*“While many companies describe climate-related risks and opportunities, few disclose the financial impact of climate change on the company.”*

Figure 6

### Artificial Intelligence Review Results (1,734 Companies)



2018 Status Report: Task Force on Climate-Related Financial Disclosures: Status Report; TCFD, September 2018