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NIRI Policy Statement -- ESG Disclosure

Background and Purpose

This policy statement, released by the NIRI Board of Directors in January 2019, articulates NIRI's views on non-financial disclosure regarding ESG (environmental, social, and governance) issues, otherwise known as "corporate sustainability." NIRI recognizes that ESG information is becoming increasingly integrated into the investment process by institutional and retail investors and encourages IR professionals to become more knowledgeable about the information and data that investors are seeking.

Over the past decade, there have been growing demands by investors, non-governmental organizations, and ratings providers for public companies to disclose metrics about the ESG-related effects of corporate operations. A meaningful increase in focus on ESG-related topics by investors during the past 18 months has led to rulemaking petitions, letters to CEOs requesting change, and updated ESG-related accounting guidelines. A significant proportion of U.S.-based institutional investors now seek and utilize ESG or sustainability data in investment screening decisions, as well as view ESG data as an additional lens on business risk.[1 2 3] BlackRock and Vanguard are among the prominent asset managers that have written public letters to companies to emphasize the importance of ESG considerations.[4] In October 2018, a coalition of law professors and public pension funds (with more than $5 trillion in assets under management) asked the Securities and Exchange Commission (SEC) to initiate a rulemaking process to require companies to provide ESG disclosure.[5] In November 2018, the Sustainability

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[1] According to the Forum on Sustainable and Responsible Investment, U.S.-based asset managers employed "SRI strategies" in their oversight of $12 trillion in professionally managed assets in 2018, a 38 percent increase from $8.7 trillion in 2016. *The Forum on Sustainable and Responsible Investment,* "US Sustainable, Responsible and Impact Investing Trends" (2018), available at: https://www.ussif.org/files/US%20SIF%20Trends%20Report%202018%20Release.pdf

[2] In the past, ESG has been a lower priority for U.S. companies. In a 2015 survey, only 30 percent of U.S.-based IR professionals said sustainability was "very important" to their company's business model, while 67 percent of IR professionals outside the U.S. said sustainability was very important to their companies. NIRI-MIT Sloan School, "Corporate Sustainability Communications Practices Report" (2015).

[3] For more data on these trends, see Pamela Styles, Next Level Investor Relations LLC, "ESG Investments Reach All-Time High: Is It Time For A Sustainability Strategy?" November 15, 2018, available at: https://www.alpha-sense.com/blog/esg-trends-2018/

[4] *See, e.g.,* BlackRock, "Larry Fink's Annual Letter to CEOs: A Sense of Purpose," January 2018, available at: https://www.blackrock.com/corporate/investor-relations/larry-fink-ceo-letter. That letter and other ESG resources can be found in the Sustainability Resources Library on NIRI's website.

[5] File No. 4-370, Cynthia Williams et al., Request for Rulemaking on Environmental, Social, and Governance (ESG) Disclosure, October 1, 2018, available at: https://www.sec.gov/rules/petitions/2018/petn4-730.pdf

Accounting Standards Board (SASB) published updated ESG accounting guidelines for 77 industry sectors.[6] [7]

One of the challenges for IR professionals in this area is that investors and other market participants use a variety of terms and acronyms, such as corporate social responsibility (CSR), socially responsible investing (SRI), sustainability, and “impact investing” to discuss their approach to ESG.[8] Interest in sustainable investing has grown from a handful of small SRI funds and religious investors in the 1980s and 1990s to include large, global asset managers. In 2007, a coalition of investors petitioned the SEC to direct companies to provide more disclosure on “greenhouse gas” emissions and climate change. Since then, investors have sought data (and/or policy changes) on an expanding array of environmental matters, such as deforestation, water use, genetically modified foods, and recycling. Other investor groups, such as the Thirty Percent Coalition, have focused on increasing gender diversity on boards and other governance issues.[9] After the Supreme Court’s *Citizens United* decision (2010), there was a surge of shareholder proposals that asked companies to provide more disclosure on political campaign contributions and lobbying expenses.

For other investors, ESG encompasses various workplace/human capital concerns, such as labor practices by overseas suppliers, pay equity, sexual harassment and whistleblower hotlines, and/or whether a company’s anti-discrimination policies include sexual orientation. The nature of environmental and social issues can vary considerably by industry sector. For instance, energy companies have been targeted by investor resolutions relating to hydraulic “fracking,” while the healthcare sector has been asked to provide more data on drug pricing or responses to the opioid crisis. Retailers have faced ongoing activism over the sale of guns as well as tobacco products.[10]

For many companies, ESG issues have become more prominent at annual meetings.[11] In recent proxy seasons, the number of shareholder proposal filings that relate to environmental and social topics has equaled or surpassed the resolutions that seek governance changes. The proxy advisor reports from Institutional Shareholder Services (ISS) and Glass Lewis & Co. now include environmental and social data, and a growing number of research firms are publishing

[6] SASB is a non-governmental organization that has invited investors and issuers to provide input on industry-specific accounting standards. SASB, Press Release: "SASB Codifies First-Ever Industry-Specific Sustainability Accounting Standards," November 7, 2018, available at: http://www.globenewswire.com/news-release/2018/11/07/1646736/0/en/SASB-Codifies-First-Ever-Industry-Specific-Sustainability-Accounting-Standards.html

[7] SASB is not affiliated with the Financial Accounting Standards Board.

[8] According to Curley Global IR, LLC, sustainability is defined as the “equal balance between environmental and social and economic considerations.” Sustainability also encompasses the various factors that “drive long-term sustainable growth at an organization.”

[9] This shareholder campaign helped inspire a 2018 California state law that requires all public companies with headquarters in the state to have a minimum number of female board members.

[10] The law firm of Sullivan & Cromwell uses the acronym, “ESP,” which stands for “environmental, social and political,” to describe these various issues. Sullivan & Cromwell, "Preparing for the 2019 Proxy Season: Practical Guidance for Directors and Board Committees," November 15, 2018, available at: https://www.sullcrom.com/files/upload/SC-Publication-Practical-Guidance-for-the-2019-Proxy-Season.pdf

[11] NIRI, *IR Update*, “Shareholder ESG Proposals on the Rise,” September 2017, pp. 10-13.

environmental and social issues ratings.[12] At the same time, the proxy advisors have become more likely to support environmental and social shareholder resolutions, which has prompted more institutional investors to support these measures, placing greater pressure on companies to respond.[13] In addition, ISS recently announced a new voting policy for the 2020 proxy season, under which it may recommend against nominating committee chairs at companies that don't have any female directors.

In addition, ESG issues can directly affect a company's reputation and are becoming a significant concern for other stakeholder groups, such as employees, potential hires, news media, customers, business partners, and local communities. The Millennial generation and a focus on "doing well by doing good" have been credited with driving this change.[14]

Overseas, at least 23 nations have enacted ESG disclosure legislation, while seven non-U.S. exchanges have adopted ESG-related listing standards.[15] Within the European Union, companies with more than 500 employees now have to provide disclosure on environmental protection, social responsibility and treatment of employees, respect for human rights, anti-corruption and bribery, and diversity on company boards.[16]

While ESG disclosure is not broadly required in the United States, many U.S.-based IR professionals already are working within their companies to provide voluntary disclosure on environmental and social issues through stand-alone reports, investor presentations, specialized sections on the company's website, SEC filings, or responses to data requests from investors or research firms.[17] However, some investors have expressed dissatisfaction over the quality and comparability of corporate ESG disclosures, complaining that too many U.S. companies are still providing "boilerplate" narratives that lack specific details relevant to their

[12] The potential influence of these ESG ratings is not limited to institutional investors. For instance, retail investors can access Sustainalytics ratings on the Yahoo Finance pages on public companies. Some companies have raised concerns about the potential conflicts of interest at ESG rating firms, particularly those firms that market advisory services to issuers on how to improve their ratings.

[13] In response to these trends, many companies have increased their off-season engagement with investors and are now addressing environmental and social topics. Investors also are seeking information on board oversight of a company's ESG or sustainability practices.

[14] *See, e.g.,* Bloomberg Intelligence, "Sustainable investing grows on pensions, millennials," April 4, 2018, available at: https://www.bloomberg.com/professional/blog/sustainable-investing-grows-pensions-millennials; EY, "Sustainable investing: the millennial investor" (2017), available at: https://www.ey.com/Publication/vwLUAssets/ey-sustainable-investing-the-millennial-investor-gl/$FILE/ey-sustainable-investing-the-millennial-investor.pdf

[15] *Hauser Institute for Civil Society at the Kennedy School, Harvard University, Initiative for Responsible Investment,* "Corporate Social Responsibility Disclosure Efforts by National Governments and Stock Exchanges," March 2015, available at: http://hausercenter.org/iri/wp-content/uploads/2011/08/CR-3-12-15.pdf

[16] European Union Directive 2014/95, available at: https://ec.europa.eu/info/business-economy-euro/company-reporting-and-auditing/company-reporting/non-financial-reporting_en

[17] The Dodd-Frank Act of 2010 included a number of specific disclosure mandates, such as rules relating to the use of gold, tin, and other African "conflict" minerals in company products as well as resource extraction payments to foreign governments.

company or industry.[18] Companies also have been criticized by some investors for allegedly overstating the sustainability of their operations, so issuers should be careful about verifying the data that they release.[19]

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NIRI encourages IR professionals to become fully aware of the types of ESG information that investors and other stakeholders are seeking from their company (as well as from peer issuers) and the disclosures that peer firms already are providing. NIRI encourages IR professionals to work closely with their company's legal counsel and internal business partners to develop a consistent approach for ESG information that will be disclosed and how that data should be verified before release. For instance, IR professionals should reach out to their company's sustainability/ESG team (if one exists), government affairs, communications, supply chain management, human resources, and any other business partners that track or maintain ESG data to fully understand how that data is collected and how it should be communicated to investors and other stakeholders. IR professionals also should be aware of their company's past ESG disclosure record and be prepared to explain to investors if the company changes how it discloses specific ESG data.

In preparing corporate SEC filings, IR professionals should work closely with their legal counsel and discourage them from providing "boilerplate" ESG disclosures. Instead, they should seek to craft company-specific narratives that include performance metrics that investors can evaluate against data from other companies.[20]

NIRI does not believe that every company should provide ESG disclosures in the same manner. The scope and nature of ESG disclosures should be based on company-specific materiality considerations and industry/sector practices. It should be determined by each company after consulting with its disclosure committee and largest investors.[21]

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[18] In a PwC survey in 2016, only 29 percent of investors expressed confidence in the quality of the ESG information they receive. According to SASB, U.S. companies still lag behind large-cap European issuers in disclosure quality. In a study of FY 2016 disclosures from 695 issuers, SASB found that 50 percent of companies provided "boilerplate" language while just 29 percent included performance metrics. *See* SASB, "The State of Disclosure 2017," December 2017.

[19] *See, e.g.,* Bloomberg News, "Investors Are Increasingly Calling Out Corporate Greenwashing," August 20, 2018.

[20] Former SEC Chair Elisse Walter shared her views on ESG disclosure in a 2017 NIRI *IR Update* commentary: "To tell the whole story, it's important to put yourself in the perspective of the investor; to ask yourself, 'What do investors want to know?' Disclosure isn't driven by what the company wants to disclose but by what the investors want to know." Elisse Walter, *IR Update*, "Witnessing an Evolution: Investors Driving Demand for Sustainability Disclosure," September 2017, p. 16.

[21] NIRI believes that SEC should continue to rely on the U.S. Supreme Court's definition of materiality when issuing new rules on ESG-related disclosure. *See* NIRI's Comment Letter on the SEC's Concept Release on the Business and Financial Disclosure Required by Regulation S-K (August 2016), available at: https://www.niri.org/NIRI/media/NIRI/Advocacy/NIRI-Comment-Letter_Disclosure-Reform_final.pdf

While some investors have urged the SEC to adopt new disclosure mandates on climate change, human capital concerns, and other public policy matters that may not be material for all companies and their investors, NIRI believes that regulators should proceed cautiously before adding to corporate disclosure burdens. It is better to wait and assess how companies respond voluntarily to investor requests on emerging disclosure issues before mandating new disclosures that may get buried in lengthy SEC filings.

Finally, IR professionals should recognize the growing importance of ESG considerations in company communications regarding long-term strategy.[22] For many investors, ESG factors are becoming a crucial component when they assess whether a company has a well-thought-out plan for long-term shareholder value. ESG disclosures may provide an opening for IR professionals and corporate executives to shift the focus away from quarterly earnings toward more thoughtful discussions about long-term strategy. They should find a more receptive audience among the company's longer-term investors, especially the growing number of passively managed index funds.[23]

Given the growing investor interest in ESG data and the evolving list of high-profile ESG concerns, NIRI plans to revisit this policy statement on a regular basis in the future. NIRI invites the IR community to provide input on how to update this statement. IR practitioners also are encouraged to visit NIRI's online Sustainability Resources Library, which has articles, reports, and webinar replays from NIRI and various third parties.[24]

Legal Disclaimer

This policy statement is intended for informational purposes only. This information is not intended to be, nor should be interpreted as, legal advice. This information in this statement should not be used for any purpose other than a summary of NIRI's views on ESG disclosure. This statement provides general information and may not reflect legal developments after the publication date. The law is changing constantly and may vary depending on a company's specific circumstances; one should consult a securities attorney for advice regarding a company's individual circumstances.

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[22] In November 2018, the CECP's Strategic Investor Initiative released a white paper on communicating long-term plans and noted the importance of ESG: "These topics are widely acknowledged as core to business success over the long-term and should be a part of an integrated discussion — not a silo or presented as a list of 'awards.'" CECP Press Release, "New Study Outlines What Institutional Investors Say Should be in a CEO's Long-Term Plan," November 8, 2018.

[23] Having discussions about a company's long-term strategy with passive funds should put a company in a more advantageous position if it is later targeted by activist funds that have shorter-term objectives.

[24] NIRI welcomes suggestions of other materials that would be appropriate for the Sustainability Resources Library, which can be found at: https://www.niri.org/resources/resource-libraries/sustainability-resources. Please send those suggestions to Ted Allen, NIRI's vice president for communications and member engagement, at tallen@niri.org.

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