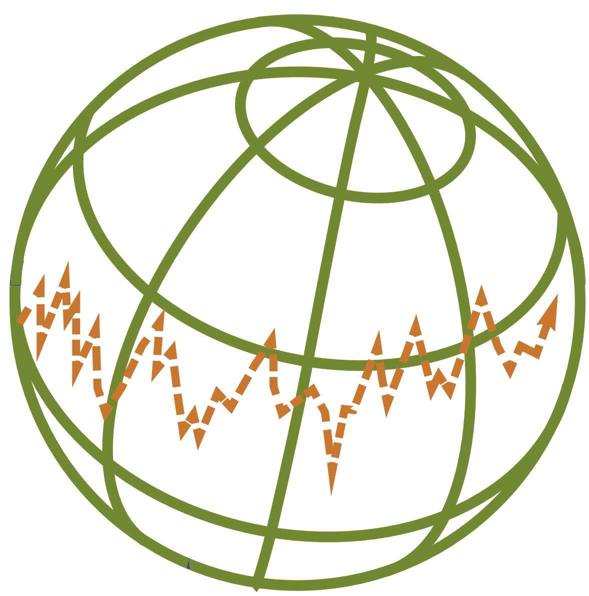
Investor Network on
CLIMATE RISK

INCR LISTING STANDARDS DRAFTING COMMITTEE CONSULTATION PAPER:

Proposed Sustainability Disclosure Listing Standard for Global Stock Exchanges

April 2013



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http://www.ceres.org/investor-network/incr/sustainable-stock-exchanges

APPENDIX A: Background—Sustainable Stock Exchanges

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Executive Summary

This paper provides the basis for a consultation process designed to help build global investor support for a listing standard for stock exchanges on corporate sustainability disclosure. The aim is to establish key elements of a minimum global standard for corporate reporting that would allow investors to access and use sustainability data, while giving companies and exchanges flexibility to address specific market regulations and cultures.

Asset owners and asset managers are asked to review and comment on the paper's recommendations by May 1, 2013.

Asset owners and asset managers are asked to review and comment on the paper's recommendations by May 1, 2013. This feedback will help shape a document with investor recommendations that NASDAQ OMX and Ceres' Investor Network on Climate Risk (INCR) will use to develop further support from global stock exchanges and the World Federation of Exchanges (WFE).

In dialogues with NASDAQ OMX and several other stock exchanges, INCR members noted that the increasing integration of sustainability issues into investment decisions is hampered by inconsistent and insufficient corporate reporting. Furthermore, many companies and exchanges cite uncertainty about the specific information investors need—and how it will be utilized—as a barrier to reporting. The need for a consistent global standard was identified in order to meet the needs of global investors, and also to help ensure that stock exchanges that adopt sustainability reporting requirements are not placed at a competitive disadvantage. Thus, NASDAQ OMX and other stock exchanges urged INCR members to develop clarity and consensus on a unified sustainability disclosure listing standard that could be adopted by all stock exchanges.

In response to these requests, the INCR Listing Standards Drafting Committee ("the Committee") was formed to draft a proposed foundation for a global standard. The Committee's recommendations provide a baseline for exchanges and were developed for all stock exchanges, regardless of size, location or familiarity with sustainability issues. They should be viewed as a proposal for a minimum standard seeking to facilitate standardization both within and between markets.

We propose three segments of a listing requirement:

1) A materiality assessment in annual financial filings where management will discuss its approach to determining the company's material environmental, social and governance (ESG) issues,

2) A hyperlink in annual financial filings to a Global Reporting Initiative (GRI) Content Index, and

3) Corporate ESG disclosure, on a "comply or explain" basis, on key ESG themes in the format and location of the company's choosing.

The background and rationale for this proposal are set out in Sections III and IV.

Consultation Process, How to Provide Comments & Timeline

We are seeking comments from investors globally on this proposal. **The initial consultation period is April 5 until May 1, 2013.**

INCR, in cooperation with other key investor networks, will host meetings to discuss the comments received and develop further investor agreement. These meetings, which will include a geographically diverse set of participants to ensure that regional needs and concerns are represented, will lead to a final investor document. Corresponding recommendations will be brought to stock exchanges and to the WFE's General Assembly and Annual Meeting in October 2013. NASDAQ OMX has committed to engaging other stock exchanges to discuss the recommendations in the lead-up to the WFE Annual Meeting. Ultimately, NASDAQ OMX (along with its Sustainable Stock Exchanges Initiative partners) will work with investors to engage the International Organization of Securities Commissions (IOSCO) to encourage the adoption of a mandatory global standard.

The Consultation Questions posed in Section V are designed to elicit feedback on key elements of the proposal. A comment template is provided as a separate attachment. It includes space for additional comments and suggestions for the proposal that are not directly captured by the Consultation Questions, and for feedback on other aspects of this paper. Respondents may also choose another format, such as a letter, to submit a response that does not specifically address the Consultation Questions. Responses should be emailed to Tracey Rembert at rembert@ceres.org, copying Erica Scharn at scharn@ceres.org. Comments will be posted to INCR's webpage at http://www.ceres.org/investor-network/incr/sustainable-stock-exchanges, and to the United Nations-backed Principles for Responsible Investment (PRI) Clearinghouse. Comments will be public and commenters will be named unless anonymity is specifically requested.

Background

The Sustainable Stock Exchanges (SSE) Initiative explores how stock exchanges, working with investors, regulators and companies, can enhance corporate transparency and performance on ESG issues, and encourages responsible long-term approaches to investment. The SSE Initiative is co-organized by the PRI, the United Nations Conference on Trade and Development, the United Nations Environment Programme Finance Initiative and the United Nations Global Compact Office.[1] Appendix A contains information about the history of the SSE Initiative.

In addition to the growing list of governments requiring sustainability or corporate social responsibility disclosures,[2] leading stock exchanges around the world are also now addressing corporate transparency and sustainability.[3] Several exchanges have amended their listing rules to mandate sustainability disclosure, and others have issued guidance or recommendations encouraging sustainability reporting. Stock exchanges have also adopted "Comply or Explain" or "Report or Explain" requirements, where companies must either provide the disclosure or explain why they do not.[4] A selection of listing standard excerpts is included in Appendix B.

Several exchanges have amended their listing rules to mandate sustainability disclosure, and others have issued guidance or recommendations encouraging sustainability reporting.

The standard global definition of sustainability is derived from the Brundtland Report (released by the UN World Commission on Environment and Development): "Sustainable development is development that meets the needs of the present without compromising the ability of future generations to meet their own needs."[5] For the purposes of this paper, "sustainability reporting" addresses the integration of environmental, social and economic considerations into corporate strategy, business practices and capital markets, as well as the key impacts on social and environmental systems that are caused by corporate activities. In this paper, ESG refers to environmental, social and governance matters related to sustainability. Governance in this context means the oversight and management of environmental and social issues—not necessarily limited to the parameters of traditional corporate governance analytics. Since the terminology still varies in the marketplace, our use of ESG is meant to encompass sustainability, corporate citizenship, corporate social responsibility and other similar terms.

Aviva Investors, which co-conceived the SSE Initiative and convened the Corporate Sustainability Reporting Coalition, put out a "call to action" in 2010 for investors to engage with exchanges in their markets on sustainability issues and helped to organize letters from PRI signatories to 30 of the largest stock exchanges in January 2011.[6] Ceres (an advocate for sustainability leadership that directs INCR) and several INCR members signed on to those letters. As part of an Aviva-led SSE

1 *See* Responsible Research, Sustainable Stock Exchanges: *A Report on Progress*, which states that a minimum level of comparability across markets is needed. In its survey of 27 stock exchanges, 80 percent of respondents welcomed a global approach to consistent and material sustainability reporting.

2 One study of 30 countries found over 140 country standards and/or laws with some form of requirement or guidance on sustainability-related reporting. *See Carrots and Sticks – Promoting Transparency and Sustainability: An Update on Trends in Voluntary and Mandatory Approaches to Sustainability Reporting.* 2010. Available online at https://www.globalreporting.org/resourcelibrary/Carrots-And-Sticks-Promoting-Transparency-And-Sustainbability.pdf

3 *See* Initiative for Responsible Investment and The Hauser Center for Nonprofit Organizations at Harvard University. *Current Corporate Social Responsibility Disclosure Efforts by National Governments and Stock Exchanges (Working Paper).* 2012. Available online at http://hausercenter.org/iri/about/global-csr-disclosure requirements

4 Benefits to stock exchanges for encouraging improved ESG disclosure and performance include: safeguarded reputation, ability to attract wider range of investors, international competitiveness, new business opportunities and potentially increased revenues, mitigation of operational risks, and support of the long-term value of listed companies. *See* EIRIS. *Sustainable Stock Exchanges: Improving ESG Standards Among Listed Companies.* 2010. Available online at http://www.eiris.org/files/research%20publications/SustainableStockExchanges2010.pdf

5 The report was released in an effort to unite countries on a common mission to pursue sustainable development together. United Nations. *Report of the World Commission on Environment and Development: Our Common Future.* 1987. Available online at http://conspect.nl/pdf/Our_Common_Future-Brundtland_Report_1987.pdf

6 Aviva Investors. *Earth Summit 2012: Towards a convention on corporate sustainability reporting at Rio+20.* 2011. Available online at http://www.aviva.com/data/media-uploads/news/File/Towards%20a%20convention%20on%20corporate%20sustainability%20reporting%20at%20Rio+20.pdf

Working Group within the PRI, North America-based INCR committed to engaging with five stock exchanges: four North American exchanges (NASDAQ OMX, NYSE of NYSE Euronext, the Bolsa Mexicana de Valores, the Toronto Stock Exchange of the TMX Group), and the Deutsche Börse.[7] Similarly, other investors volunteered to engage with exchanges in their region or exchanges they hold in their investment portfolios. The INCR SSE Working Group was formed in early 2011 to convene a group of INCR members on a monthly basis to coordinate engagement with these stock exchanges regarding corporate sustainability reporting and listing standards. In response to requests from several exchanges for clarity around a listing standard, the INCR SSE Working Group launched the Committee in October 2012 to develop a minimum set of investor expectations. The INCR SSE Working Group continues to coordinate with the PRI and other groups to share best practices and lessons learned from these market-specific engagements with exchanges.

Investors are involved in a number of other global ESG disclosure initiatives, including the following:

Global ESG Disclosure Initiatives

Initiative	Objective	Scope
CDP (formerly the Carbon Disclosure Project)	"To provide a global system for companies and cities to measure, disclose, manage and share vital environmental information" [CDP sends questionnaires to companies seeking information on climate change, water, supply chains and forestry]	Global
Global Initiative for Sustainability Ratings (GISR)	"To transform the definition of corporate value such that markets reward the preservation and enhancement of all forms of capital: human, financial intellectual, natural and social"	Global
Global Reporting Initiative (GRI)	"Provides all companies and organizations with a comprehensive sustainability reporting framework"	Global
The International Integrated Reporting Council (IIRC)	"Promoting integrated reporting, a concise communication about how an organization's strategy, governance, performance and prospects lead to the creation of value over time"	Global
The Prince's Accounting for Sustainability Project (A4S)	"To help ensure that sustainability—considering what we do not only in terms of ourselves and today, but also of others and tomorrow—is not just talked and worried about, but becomes embedded in organizations' 'DNA' "	Global
Project Delphi	"Convergence on accepted methodologies for measuring and reporting ESG activity by companies and investors. Validation of materiality of 'super-factors' and their metrics"	Europe
Sustainability Accounting Standards Board (SASB)	"Development and dissemination of industry-specific sustainability accounting standards" [for use in U.S. securities filings]	U.S.
United Nations Environment Programme Finance Initiative (UNEP FI)	"Understanding the impacts of environmental and social considerations on financial performance"	Global
United Nations Global Compact (UNGC) [& its Communication on Progress reporting requirements]	"Commitment to aligning business operations and strategies with universally accepted principles in the areas of human rights, labour, environment and anti-corruption"	Global

7 Deutsche Börse was included due to its merger with NYSE Euronext under consideration at the time.

The proposed listing rules and recommendations for exchanges are intended to help build a foundation for a sustainability listing standard, incorporating elements from several of these initiatives, and are not intended to preempt or explicitly endorse any one of them as they are being developed and refined. These initiatives are viewed as a strong resource for stock exchanges as they implement the proposed listing recommendations and build on them for their particular needs.

Context, Materiality & Key Performance Indicators

CONTEXT

The proliferation of sustainability surveys, rankings, products, lists, standards and advertising is indicative of mainstream market interest in sustainability—and an appreciation that sustainability issues have financial significance for investors.[8]

An increasing number of investors consider ESG factors to be material, and have been calling for greater ESG-related disclosure from companies for years.[9] While voluntary sustainability reporting continues to grow each year, only about 3,400 companies published a sustainability report as of 2011, and few companies discuss material ESG information in their financial filings.[10] In 2008, Bloomberg—a provider of data and analytics for the financial community—began collecting and publishing corporate ESG data for 3,000 publicly traded companies (which rose to 5,217 in 2011), drawing on publicly disclosed ESG information. Currently, more than 120 ESG indicators are displayed alongside mainstream financial indicators for Bloomberg's 300,000 customers. There is significant interest in Bloomberg's ESG data: in the second half of 2010, 5,000 unique customers in 29 countries accessed more than 50 million ESG indicators. The number of users of the ESG data increased by 50% in 2011 over 2010, but only represents about 1% of the total user base. Bloomberg states that data quantity and quality remain the primary barriers to integration by mainstream users.[11]

8 *See* Global Initiative for Sustainability Ratings (GISR). http://ratesustainability.org/; PricewaterhouseCoopers LLP (PwC). *Do Investors Care About Sustainability? Seven trends provide clues.* 2012. Available online at http://www.pwc.com/en_US/us/corporate-sustainability-climate-change/assets/investors-and-sustainability.pdf

9 The growth of investor networks such as the PRI is a clear indication of this: PRI has 1,170 signatories with over $30 trillion in assets under management. Signatories work together to implement Principles for Responsible Investment, which reflect the view that ESG issues can affect the performance of investment portfolios. CDP, on behalf of 722 investor signatories managing $87 trillion in assets (a third of the world's invested capital), sends questionnaires to 5,000 companies annually requesting information on climate change strategy and greenhouse gas emissions. Investor signatories to CDP surveys on water, forestry and supply chains continue to climb as well. More than 4,100 companies use CDP to report their climate-related strategies and impacts, and of the world's largest public companies, 81 percent use CDP to disclose their environmental and natural resources-related impacts. Further evidence of the mainstreaming of corporate ESG data: On the main summary page for every company, Google Finance lists the company's Carbon Disclosure Rating. *Also see*, US SIF (formerly Social Investment Forum). *Rulemaking Petition.* 2009. Available online at https://ussif.org/documents/ESG_Letter_to_SEC.pdf

10 Notably, sustainability reporting varies widely by market: a 2011 KPMG study found that 95 percent of the 250 largest companies in the world report sustainability information—but two-thirds of non-reporters are U.S.-based. *See* KPMG. *KPMG International Corporate Responsibility Reporting Survey 2011.* 2011. Available online at http://www.kpmg.com/Global/en/IssuesAndInsights/ArticlesPublications/corporate-responsibility/Documents/2011-survey.pdf

11 Bloomberg. *The Sustainability Edge: Sustainability Update 2011.* 2012. Available online at http://www.bloomberg.com/bsustainfiles12/images/report_2011/2011_BloombergSustainabilityUpdate.pdf. Notable quote from this report: "Disclosure leads to benchmarking and best practices–and drives competition which fuels innovation….We invested in these assets because sustainability issues are material to all of our partners."

Accountants, securities regulators, credit rating agencies, data providers, consultants and other key capital market players are also recognizing the connection between ESG issues and companies' financial value.[12] Accounting groups, including the International Accounting Standards Board, the Financial Accounting Standards Board and the Canadian Institute of Chartered Accountants[13] are publishing guidance documents to help companies interpret materiality in the context of ESG disclosure and accounting conventions. In 2010, the U.S. Securities and Exchange Commission issued interpretive guidance relating to material risks presented by climate change,[14] and the Canadian Securities Administrators published Environmental Reporting Guidance, which clarifies how environmental risks, including climate change, may be material.[15] Credit rating agency Standard and Poor's updated its management and governance rating criteria in November 2012, to specifically reference environmental and social factors as areas of material risk that can affect a debt issuer's credit quality.[16]

In this context, we provide key considerations on Materiality and Key Performance Indicators that form the basis for our recommendations in Section V.

MATERIALITY

In order to make fully informed investment decisions, investors need standardized information that can be used to measure company performance over time and against peers. Current interpretations of materiality produce varying disclosures with significant gaps, which poses risks to investors.[17] In the U.S., a fact or issue is deemed to be material if there is a substantial likelihood that a reasonable person would consider it important, and if a reasonable investor would view it as significantly altering the 'total mix' of available information.[18] Consistent with this approach, the International Federation of Accountants states that "misstatements, including omissions, are considered to be material if they, individually or in the aggregate, could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements."[19] See Appendix C for materiality definitions and resources.

A purely risk-based disclosure regime fails to provide investors with consistent information on ESG policies, management systems and performance over time—all key considerations for evaluating a company's ESG performance and the quality of its management. The short-term focus of most corporate reporting further exacerbates this problem as ESG issues pose short-, medium- and long-term risks and opportunities. Other significant ESG risks may fall into an 'indeterminate' timeframe.[20]

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12 *See* The Prince's Accounting for Sustainability Project (A4S). *Future Proofed Decision Making: Integrating environmental and social factors into strategy, finance and operations.* 2012. Available online at http://www.accountingforsustainability.org/wp-content/uploads/2011/10/A4S-Report-Future-proofed-decision-making.pdf

13 Canadian Institute of Chartered Accountants (CICA) and Canadian Performance Reporting Board (CPRB). *Building a Better MD&A: Climate Change Disclosures.* 2008. Available from http://www.cica.ca/research-and-guidance/mda-and-business-reporting/mda-publications/item12846.pdf

14 United States Securities and Exchange Commission (SEC). *Commission Guidance Regarding Disclosure Related to Climate Change*, 17 CFR Parts 211, 231 and 241. 2010. Available online at http://www.sec.gov/rules/interp/2010/33-9106.pdf

15 Canadian Securities Administrators (CSA). *CSA Environmental Reporting Guidance*, CSA STAFF NOTICE 51-333. 2010. Available online at http://www.osc.gov.on.ca/documents/en/Securities-Category5/csa_20101027_51-333_environmental-reporting.pdf

16 Standard & Poor's. "How we rate management and governance factors." 2012. Available online at http://www.standardandpoors.com/spf/upload/Ratings_US/Managment_Governance_Criteria_2.pdf

17 Although the perspectives of investors and other users of corporate financial statements have changed dramatically over time, the scope and quality of corporate disclosures regarding ESG issues have not.

18 U.S. Securities and Exchange Commission (SEC). Staff Accounting Bulletin: No. 99—Materiality. 17 CFR Part 211. August 12, 1999. Available online at http://www.sec.gov/interps/account/sab99.htm

19 International Federation of Accountants (IFAC). *International Auditing and Assurance Standards Board (IAASB) International Standard on Auditing (ISA) 320: Materiality in Planning and Performing an Audit.* Available online at http://www.ifac.org/sites/default/files/publications/files/A019%202012%20IAASB%20Handbook%20ISA%20320.pdf

20 Lydenberg, Steve. On Materiality and Sustainability: *The Value of Disclosure in the Capital Markets.* (Cambridge, MA: Initiative for Responsible Investment) 2012. Available online at http://hausercenter.org/iri/wp-content/uploads/2010/05/OnMateriality_Final.pdf

Current practice in financial reporting generally fails to capture many ESG-related risks and externalities that would help investors gauge risks to individual companies, as well as understand each company's contribution to or impact from systemic risks. Systemic risks are risks to the overall resiliency of the systems we depend upon (economic, social and environmental).[21] Reporting that focuses exclusively on risks and opportunities to the issuer implicitly omits any discussion of risks and opportunities issuers present to others. Institutional investors, many of which have long-term investment horizons and are often invested across the economy, are particularly exposed to the systemic risks presented by short-term thinking and undisclosed externalities, as demonstrated by the global financial and climate crises.[22]

Mandating a materiality assessment on ESG issues in financial filings is necessary to address these concerns and to make it clear that material ESG matters are required to be included in financial reporting. Only when ESG information is universally reported in one of the main sources of information used regularly by all investors and analysts—financial reports—will capital markets be able to value companies based on more than a narrow set of financial indicators that give a limited picture of risk and opportunity.

KEY PERFORMANCE INDICATORS (KPIs)

Several stock exchanges asked for a list of recommended sustainability Key Performance Indicators (KPIs) common to several markets. KPIs for ESG matters are rapidly evolving, and should be developed through a multi-stakeholder process; as such, exchanges and issuers should refer to both well-established and developing standards for KPIs, and are encouraged to monitor the initiatives that are currently developing sector-specific KPIs. Several of these initiatives and resources related to KPIs are described in Appendix D.

Appropriate ESG KPIs vary by sector, industry, sub-industry and market based on the key sustainability challenges faced by each.[23] Additionally, an "indicator" can be a single data point, such as a percentage of revenues from a particular business line, or a set of data points accompanied by narrative disclosure, such as information relating to labor conditions in a corporation's manufacturing supply chain.[24]

Rather than propose a set of minimum KPIs, we provide a list of common ESG disclosure areas frequently used by investors in their corporate assessments to serve as a baseline for company reporting. These general subject areas are often under-represented in corporate disclosures and inconsistently reported, but are relevant to most companies across markets and industries. The categories are broad enough to allow companies the flexibility to report relevant KPIs under each category and a large number of potential KPIs fit into each of the subject areas.

21 *Ibid.*

22 *See* Principles for Responsible Investment (PRI). *Building the capacity of investment actors to use environmental, social and governance (ESG) information.* 2013. Available online at http://www.unpri.org/viewer/?file=wp-content/uploads/20130305PRI_CIA_ESG_Capacity_Building_Report.pdf; *Also see*, Principles for Responsible Investment (PRI). *Integrated Analysis: How investors are addressing environmental, social and governance factors in fundamental equity valuation.* 2013. Available online at http://www.unpri.org/viewer/?file=wp-content/uploads/Integrated_Analysis_20131.pdf

23 *See* Lydenberg, Steve, Jean Rogers, and David Wood. *From Transparency to Performance: Industry-Based Sustainability Reporting on Key Issues.* (Cambridge, MA: Initiative for Responsible Investment) 2010. Available online at http://hausercenter.org/iri/wp-content/uploads/2010/05/IRI_Combined_KPI.pdf

24 *See* Society of Investment Professionals in Germany (DVFA) and The European Federation of Financial Analysts Societies (EFFAS). *KPIs for ESG—Guidelines for the Integration of ESG into Financial Analysis and Corporate Valuation (version 3.0).* 2010. Available online at http://www.effas-esg.com/wp-content/uploads/2011/07/KPIs_for_ESG_3_0_Final.pdf

Elements of Proposed Listing Standard

This section presents a proposal for a listing standard on sustainability disclosure. The proposal contains ***mandates*** for the minimum disclosures that investors feel stock exchanges should require, ***guidance and recommendations*** related to those mandates, and ***recommendations for exchanges*** in the implementation of such items.[25] Consultation Questions are listed throughout.

1) MATERIALITY ASSESSMENT (M1): Every company will discuss its process for determining the ESG factors material to its business, as well as the outcome of this materiality assessment, within its annual financial filings. The four key components of the materiality assessment are as follows:

1A) Companies will discuss how they determined their material ESG issues

1B) Companies will discuss who was involved in that process (including groups of stakeholders consulted, internal teams, and key management and board oversight)

1C) Companies will disclose which ESG issues were determined to be material and why, including a discussion of both the risks and opportunities each issue presents as well as its connection to financial performance and business strategy

1D) Companies will periodically review the materiality assessment, update as necessary, and report on the frequency of scheduled reviews.

Mandate Guidance:

A materiality assessment is the critical first step to understanding the various ways ESG factors may impact corporate value—both positively and negatively—and will facilitate efficient allocation of resources to manage risks and take advantage of opportunities.[26] As such, this core disclosure is appropriate for all companies, including those that are not familiar with sustainability issues and have never reported any ESG-related information. The emphasis placed upon the materiality determination process will help companies to focus their ESG reporting efforts and increase the information's decision-making value.[27] Completion of the requirements of this mandate will also prepare companies to respond to other ESG reporting requirements.

25 Recommendations are placed under the applicable mandate, followed by the recommendations for exchanges. .

26 Ceres. *The 21st Century Corporation: The Ceres Roadmap to Sustainability.* 2010. Available online at www.ceres.org/resources/reports/ceresroadmap-to-sustainability-2010

27 Deloitte. *Disclosure of Long-term Business Value: What Matters.* 2012. Available online at http://www.deloitte.com/assets/Dcom-UnitedStates/Local%20Assets/Documents/us_scc_materialitypov_032812.pdf

1B: Companies should consider using stakeholder mapping—the process by which companies identify stakeholders and understand, track and assess ESG-related engagements with each group. Mapping assists the company in ensuring that a broad range of stakeholders are engaged in the process and in determining the appropriate depth of engagement for certain groups. Mapping is also an opportunity to identify the stakeholders that are best positioned to provide expert feedback on the company's ESG disclosures, including any relevant KPIs. Some companies find it useful to develop a materiality matrix to help identify and prioritize key ESG issues. A materiality matrix categorizes issues on two dimensions, such as the importance to stakeholders and society and the extent of the current or potential impact on the company.[28]

1B: Board oversight and commitment, as well as management systems and processes, should be established in order to fully integrate sustainability into the business.

1B: Stakeholders are individuals or groups within or outside the company who are affected by, or can affect, the company's activities. Stakeholders of a company include investors, the Board of Directors, employees, suppliers, government, communities, customers and non-governmental organizations, among others. The emphasis on stakeholder engagement will help the company identify hidden risks and prioritize the most material issues for the company.

1D: Investors need to know that companies are accounting for emerging issues, industry best practices, shifting policy and economic contexts, and stakeholder expectations. Companies should review their materiality assessment annually and update as necessary.

? Consultation Questions:

Q1: Are there any strong reasons not to mandate the materiality discussion?

Q2: Should the materiality assessment explicitly include short-, medium- and long-term, as well as 'indeterminate,' timeframes for reporting risks and opportunities?

Q3: Are there additional ways to address the lack of ESG risk reporting in financial filings?

NOTE: M2 does not mandate or endorse a GRI-based sustainability report, and completion of a GRI Content Index does not require the publication of a GRI-based report. The G3.1 Content Index—the most current version at publication of this paper—is included in Appendix E.

2) GLOBAL REPORTING INITIATIVE (GRI) CONTENT INDEX (M2): Every company will provide a hyperlink in its annual financial filings to a GRI Content Index, which will inform investors about the availability and location of a company's ESG data.

A key impetus for investors engaging with stock exchanges on ESG disclosure was their frustration over the inconsistencies of ESG reporting, and the time-consuming task of locating any company's ESG reporting items spread across numerous reporting vehicles. A GRI Content Index will address this concern by eliciting, for each GRI KPI, whether the disclosures exist from a given company, and where they can be found.

28 *See* Ceres, *The 21st Century Corporation: The Ceres Roadmap to Sustainability*

Mandate Guidance:

The GRI Content Index currently contains the most comprehensive, widely used set of ESG indicators. It will provide companies with guidance on a broad range of ESG indicators from which to select and report, to fulfill the mandates and recommendations in the listing standard. For each disclosure item in the Index, companies indicate Level of Reporting (response options are Fully, Partially or Not Reported) and Location of Disclosure.[29]

The GRI Guidelines on which the Content Index is based meet the basic tests of credibility and legitimacy. The Guidelines were developed through an international multi-stakeholder process that includes investors, issuers, non-governmental organizations and public comment opportunities. GRI has been developing indicators for more than a decade.

RECOMMENDATION FOR EXCHANGES IN THE IMPLEMENTATION OF M2:

The World Federation of Exchanges (WFE) should assess the applicability of the GRI Content Index every five years to account for new developments and evolving standards around ESG metrics. The WFE review of the GRI Content Index, rather than reviews conducted by individual exchanges, will ensure consistency across exchanges and markets.

Consultation Questions:

Q4: Is the GRI Content Index the best way to give investors some disclosure consistency without being overly prescriptive for companies? If not, please list other suggestions.

Q5: Would it be preferable to include the GRI Content Index itself in financial filings, rather than a hyperlink to it?

Q6: Should something other than the hyperlink to the GRI Content Index be included in the financial filings? If so, what and why?

Q7: Is five years an appropriate timeframe for the periodic review of the GRI Content Index and developments in the market?

3) CORPORATE ESG DISCLOSURE (M3): Every company will disclose information on the following categories of ESG issues, using a comply or explain approach for each category:

- Climate change
- Diversity
- Employee relations
- Environmental impact
- Government relations
- Human rights
- Product impact and safety
- Supply chain

29 Global Reporting Initiative (GRI). *Sustainability Reporting Guidelines—Version 3.1 (G3.1)*. 2011. Available online at https://www.globalreporting.org/resourcelibrary/G3.1-Guidelines-Incl-Technical-Protocol.pdf

Issuers will determine the format and location of the reporting, which could include one or more of the following: stand-alone sustainability reports, annual reports, financial filings, integrated reports, websites and other venues.

Mandate Guidance:

The corporate ESG disclosures will allow investors to gauge issuer performance over time. Comprehensive disclosures on the aforementioned categories should include both qualitative and quantitative information and should ideally incorporate the following aspects: policies and procedures, performance data (including regulatory fines and other legal actions), goals and timeframes, and related governance.

Examples of reporting topics in each category are provided below (note that these examples are provided for illustrative purposes and should not be considered to be an exhaustive list, or a set of minimum requirements) and background information is contained in Appendix D:

- **Climate change:** greenhouse gas emissions and reduction initiatives, physical risks and opportunities
- **Diversity:** employee, board and supplier diversity; training and recruitment programs
- **Employee relations:** labor relations and freedom of association, safety, employee turnover and demographics, training, remuneration
- **Environmental impact:** water, energy and materials consumption; emissions and waste; toxins; packaging
- **Government relations:** political involvement and spending, contracting and revenue payments, tax strategy
- **Human rights:** non-discrimination efforts, prevention of child and forced labor, compliance with international human rights norms
- **Product impact and safety:** cultural and community impacts, product life cycle assessments, recalls, product integrity and safety
- **Supply chain:** size and geographic scope, risks of disruptions (due to e.g. extreme weather events, labor disputes, etc.), impacts on local communities, labor and environmental compliance efforts

M3 RECOMMENDATION:

Financial and ESG data are often reported to investors using different timeframes and/or reporting cycles and it is important that both sets of disclosures be aligned in the future, to avoid confusion and inaccurate analytics. Reporting timeframes should be aligned within three to five years of the implementation of the listing rule.

Aligning reporting timeframes is an essential element to moving forward with the integration of financial and ESG information and the integration of sustainability into both business and investor decision-making. A timeframe of three to five years will provide companies with sufficient time to develop processes and align reporting regimes.

Consultation Questions:

Q8: Should the exchanges, rather than the issuers, determine the format and location of the sustainability reporting?

Q9: Do you agree with the current list of ESG issues and examples? If not, what ESG categories would you suggest removing or adding?

Q10: Is three to five years an appropriate timeframe for aligning reporting timeframes and if not, how long should it be?

Q11: Are there situations where it would not be appropriate to synchronize financial and sustainability reporting timeframes, and if so, what are those situations?

GENERAL RECOMMENDATION FOR ISSUERS

ASSURANCE

Data presented in the company's ESG disclosures should be independently assured within five to seven years of the listing requirement's issuance.

An independent and credible third party should verify key ESG data. Assurance is an evaluation method that utilizes a specified set of principles and standards to assess the quality of data and underlying systems. Verification, auditing and validation are some of the tools and processes by which assurance is obtained. Assurance is necessary because it enhances the credibility and reliability of the reported information, increases investor confidence in the accuracy of the information,[30] and can improve the usefulness and effectiveness of the information being presented.[31] There are indications that investors and other stakeholders are paying attention to verification information for ESG data.[32] However, implementation of independent assurance varies widely across markets,[33] requires an investment in data collection processes, and requires qualified assurers. Five to seven years should allow companies to instill processes for good data collection and for creating demand for third-party services.

30 *See*, e.g., the International Corporate Governance Network's statement that companies should adopt and report on their policy towards obtaining assurance. International Corporate Governance Network (ICGN). *ICGN Statement and Guidance on Non-financial Business Reporting.* 2008. Available online at https://www.icgn.org/files/icgn_main/pdfs/best_practice/buss_reporting/icgn_statement_&_guidance_on_non-financial_business_reporting.pdf; *Also see*, The International Integrated Reporting Council (IIRC). *Towards Integrated Reporting: Communicating Value in the 21st Century—Summary of Responses to the September 2011 Discussion Paper and Next Steps.* 2011. Available online at http://theiirc.org/wp-content/uploads/2012/06/Discussion-Paper-Summary1.pdf

31 *See* AccountAbility. *AA1000 Assurance Standard 2008.* 2008. Available online at http://www.accountability.org/images/content/0/5/056/AA1000AS%202008.pdf; International Federation of Accountants (IFAC). *International Auditing and Assurance Standards Board (IAASB) International Standard on Assurance Engagements (ISAE) 3000 (Revised), Assurance Engagements Other Than Audits or Reviews of Historical Financial Information.* Exposure draft 2011. Available online at http://www.ifac.org/sites/default/files/publications/exposure-drafts/IAASB_ISAE_3000_ED.pdf
Social Accountability International (SAI). *SA8000 Standard: 2008.* 2008. Available online at http://www.sa-intl.org/_data/n_0001/resources/live/2008StdEnglishFinal.pdf; Verite. *Standards for the Knowledge and Skills of Social Auditors.* 2009. Available online at http://www.verite.org/sites/default/files/images/Standards_for_the_Knowledge_and_Skills_of_Social_Auditors_October_2009_0.pdf

32 In a study looking at the almost 44 million total "hits" to the ESG metrics in the Bloomberg database in three periods from 2010-2011 (a "hit" is when a user accesses one of these data points), Verification Type (which indicates whether the company's ESG policies were subject to an independent assessment for the reporting period) was in the list of top 20 metrics of greatest interest to the market on a global basis. *See* Eccles, Robert G., Michael P. Krzus, George Serafeim. "Market Interest in Nonfinancial Information" (Fall 2011). *Journal of Applied Corporate Finance*, Vol. 23, No. 4, pp. 113-127, 2011. Available online at http://www.mikekrzus.com/downloads/files/JACF-Market-interest.pdf

33 For example, sustainability reports with assurance statements are much more common in Europe; only 14% of sustainability reports in the U.S. have assurance statements, compared to 73% in France. *See* Eccles, Robert G. *One Report: Integrated Reporting for a Sustainable Strategy in Harvard Business School Faculty Research Symposium: Executive Summaries.* May 20, 2010. Available online at http://hbswk.hbs.edu/pdf/research.sym.eccles.pdf

Consultation Questions:

Q12: Is an assurance requirement appropriate for all markets?

Q13: Is the recommended time frame of five to seven years sufficient or too long or too short?

Q14: Should the recommendation be more specific in terms of what should be assured?

ADDITIONAL RECOMMENDATIONS FOR EXCHANGES IN THE IMPLEMENTATION OF THE LISTING STANDARD

SIZE OF COMPANIES

Large issuers (as determined by the exchange) are expected to comply with all three mandates upon passage. If exchanges determine that smaller companies will require more time for compliance with these mandates, exchanges should set the market capitalization threshold and the maximum timeframe for compliance to achieve the goal of all companies reporting within a reasonable timeframe of three to five years. However, if items are material, they must be disclosed regardless of size.

Smaller companies tend to disclose less information and to have less developed systems for managing ESG issues, despite the unique risks and opportunities that they face, so it is important to have the listing standard apply to all companies. However, smaller companies may need more time to comply since they have fewer employees and resources. Since market capitalization definitions and the proportion of listed companies in each size category vary by market and by exchange,[34] stock exchanges should choose their market capitalization thresholds for a phase-in period for small companies, if needed.

Consultation Questions:

Q15: Should small companies be granted additional time, and if so, how much is sufficient?

EXCHANGE MONITORING OF REPORTING

A) Stock exchanges are strongly encouraged to assess the overall level of disclosure and reporting quality of the mandated disclosures (materiality assessment, GRI Content Index and corporate ESG reporting) after two years and every three years thereafter to reassess quality. If quality is poor, the exchange(s) should intervene and recommend best practices or means of improvement to ensure usefulness to shareholders and the market.

B) Each exchange is strongly encouraged to report publicly on its parameters for the oversight of the monitoring process, the methodology employed, and the outcomes of the assessment.

C) Exchanges are encouraged to seek investor feedback on the quality of the disclosures.

34 *See* World Federation of Exchanges (WFE). *2011 Annual Report*. Available online at http://www.world-exchanges.org/files/statistics/excel/WFE2011.pdf (WFE 2010 Domestic Market Segmentation Survey, page 39); World Federation of Exchanges (WFE). *2012 WFE Market Highlights: No 239—January 2013*. Available online at http://www.world-exchanges.org/files/focus/pdf/focus_january.pdf (WFE Market Statistics, page 39)

Consultation Questions:

Q16: Is the proposed timeframe reasonable (two years followed by every three years)? If not, what timeframe do you recommend for reviewing disclosures?

Q17: Who should conduct the review? Should the WFE or an independent third-party conduct reviews of the disclosure quality instead?

Q18: Is there any advice investors can offer on implementation of this monitoring recommendation?

MARKET ALIGNMENT

A) Exchanges should work together in each market to make sure that each of a country's exchanges is providing consistent rules and guidance for corporate ESG reporting and the materiality assessment.

B) Stock exchanges—either individually or in cooperation with other exchanges in their markets—should evaluate the ESG categories in M3 and decide whether to develop or recommend KPIs (under the proposed ESG categories or in additional ESG categories) that are pertinent to their specific markets and distribution of industries.

ISSUER EDUCATION AND CAPACITY BUILDING

A) Stock exchanges are encouraged to develop expertise and resources to review and evaluate ESG reporting standards on a regular basis.

B) Stock exchanges are encouraged to provide guidance and training on their ESG listing standards to issuers from the outset and on an ongoing basis.

C) Stock exchanges are encouraged to host educational and training sessions for issuers on best practices for materiality assessments and ESG reporting. Training should include stakeholder input. [Several leading stock exchanges, including BM&FBOVESPA, Hong Kong Exchanges and Clearing Ltd., NYSE, and Singapore Stock Exchange have held well-attended and successful seminars and workshops for issuers.] Exchanges should also provide issuers with guidance on ESG reporting and resources, such as Frequently Asked Questions.

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This document presents the consensus achieved by the Drafting Committee and should not be construed to represent the views of all INCR members.

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