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ABA Section of Environment, Energy and Resources

Environmental Disclosure Committee Newsletter

Vol. 6, No. 1 March 2009

MESSAGE FROM THE CHAIR

Greg Rogers

The Environmental Disclosure Committee focuses on four interrelated areas of environmental accounting and disclosure: (1) generally accepted accounting principles (GAAP) relating to environmental costs, assets, liabilities, and impairments; (2) disclosure of environmental liabilities and risks under Securities and Exchange Commission (SEC) regulations; (3) the requirements of Sarbanes-Oxley as they relate to environmental accounting and disclosure; and (4) voluntary environmental/sustainability reporting. In light of recent developments described in this newsletter, the Committee may now need to add a fifth area of focus—*enforcement of state securities laws*.

This newsletter contains three articles on climate change and sustainability disclosure. Read together, they give a broad perspective of the internal and external forces driving companies towards greater transparency on environmental and social matters.

In our first article, Seth Kerschner describes the agreement of Xcel and Dynegy to provide expanded disclosures on climate risk in recent settlements with the New York Attorney General Andrew Cuomo. The settlements followed the issuance of subpoenas to Xcel, Dynegy, and three other utility companies in September 2007 under the authority of the state's securities laws, in which the attorney general sought to gather information regarding the companies' analyses of climate change risks and the disclosure of those risks to investors. These settlements are the first binding agreements between government and private industry regarding climate change disclosure. Cuomo expects the settlements to set "a new industry-wide precedent that will force companies to disclose the true financial risks that climate change poses to their investors." If Cuomo is right, the settlements may be a watershed event marking the shift from voluntary to mandatory disclosure. *Will efforts to make voluntary disclosure mandatory, if successful, eliminate the need for voluntary disclosure?*

In light of the Xcel and Dynegy settlements, many organizations are seeking additional guidance and a consistent structure for climate change disclosures in financial reports, a need thus far ignored by the SEC. Companies that want to provide more information on climate risk, but are unsure how to do so, will benefit from a forthcoming standard from ASTM. In our second article, Lewis Jones describes the draft ASTM standard on climate change disclosures released for public comment in November 2008. The ASTM guide purports to be voluntary, but Jones notes that the drafters are well aware that many other ASTM standards have become mandatory after being adopted by other organizations, including regulatory agencies. Might New York Attorney General Andrew Cuomo require conformance with this ASTM standard in future settlements, or will widespread adoption of a new ASTM standard allow Cuomo to focus his attention elsewhere? *Will increased voluntary disclosure eventually render regulatory disclosure moot?*

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Kevin J. Klesh, Editor

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In the last article, *Modern Due Diligence: Opportunities and Challenges in the Green Economy*, Mike Wallace and Michael Berg contend that companies can reap significant benefits from increased disclosure if they do it right. They cite as an example a biotechnology firm that opened up new opportunities to attract investment, talent, and customers by positioning itself on the Dow Jones Sustainability Index. They report that the company, which was already accustomed to issuing sustainability reports, was able to better leverage its existing disclosure efforts by focusing more closely on investor relations versus other interest groups. *What environmental information is material to investors?*

Our appreciation goes to the authors and to our Newsletter vice chair, Kevin Klesh. I hope you find this newsletter valuable and encourage you to let us know how we can best serve your continuing education needs in the area of environmental disclosure.

POWER COMPANIES AGREE TO EXPANDED DISCLOSURE OF CLIMATE CHANGE RISK IN LANDMARK SETTLEMENTS WITH NEW YORK ATTORNEY GENERAL

Seth Kerschner

Introduction

Two of the largest emitters of greenhouse gases (GHGs) recently agreed to provide investors with detailed information on the financial risks posed by climate change. On Aug. 26, 2008, the New York Attorney General's Office entered into a settlement agreement with Xcel Energy, Inc. (Xcel) whereby Xcel agreed to include an analysis of the financial and physical impacts of climate change on the company's operations in its public filings with the Securities and Exchange Commission (SEC). And on Oct. 23, 2008, Dynegy Inc. (Dynegy) entered into a similar agreement with the New York Attorney General's Office.

These settlements follow the issuance of subpoenas to Xcel, Dynegy, and three other utility companies in September 2007, in which the Attorney General sought to gather information regarding the companies' analyses of climate change risks and the disclosure of those risks to investors. These power companies were in various stages of constructing new coal plants at the time the subpoenas were issued.

The settlements are important because they are the first binding agreements between government and private industry regarding climate change disclosure. Furthermore, New York Attorney General Andrew Cuomo has indicated that his office expects the settlements to set "a new industry-wide precedent that will force companies to disclose the true financial risks that climate change poses to their investors." Xcel was the fifth largest emitter of GHG emissions among utilities in the United States in 2006, according to the settlement. Dynegy will also become one of the top five emitters of GHG emissions in the United States as a result of its operation of eight new proposed coal-fired plants, according to a letter from the Attorney General's Office accompanying the September 2007 subpoena.

Detailed Disclosure on the Impacts of Climate Change Required

Pursuant to its settlement, Xcel agreed to (i) analyze how it is impacted by existing and potential GHG legislation in jurisdictions where it operates, (ii) describe the impacts of GHG litigation in jurisdictions where it operates, (iii) analyze financial risks to the company from physical impacts associated with climate change, (iv) provide the company's current position on climate change, (v) disclose its current and future estimated GHG emissions along with its plans for reducing GHG emissions, and (vi) report on its corporate governance activities related to climate change.

Dynegy's settlement is substantially similar to Xcel's. However, Dynegy agreed to specifically disclose the impact of the Regional Greenhouse Gas Initiative (RGGI) on its operations. RGGI is a cooperative effort by ten Northeast and Mid-Atlantic states to limit GHG emissions from the power generation sector through a multi-state GHG cap and trade program. It is likely that Dynegy's settlement specifically mentioned RGGI because Dynegy has operations in Northeastern states that are subject to RGGI, while Xcel operates in Western and Midwestern states that are not part of RGGI.

The settlements specify that the required disclosures are to be made in the power companies' 10-Ks. However, it is expected that Xcel and Dynegy will include these discussions in the sections of its filings covering four key areas. These areas include (i) Risk Factors, (ii) costs of environmental compliance pursuant to Item 101 of Regulation S-K, (iii) material legal proceedings pursuant to Item 103 of Regulation S-K, and (iv) management discussion and analysis of trends, uncertainties or events reasonably expected to affect the company pursuant to Item 303 of Regulation S-K. If the settlements set the new precedent across the power generating industry that Cuomo expects them to, Xcel and Dynegy's publicly traded peer companies in the power generation industry may also need to review and revise their SEC disclosures either in response to, or in anticipation of, similar calls for greater climate change disclosure.

Subpoena Issued Under State Blue Sky Law

The Attorney General issued the subpoenas to the power companies under the Martin Act, a state securities law that grants the Attorney General broad powers to subpoena records in order to protect investor interests. In letters accompanying the subpoenas, the Attorney General expressed concern that the power companies had not adequately disclosed the increased financial, regulatory, and litigation risks that will come with the increase in emissions from the operation of new coal-fired power plants.

The Martin Act is New York's 1921 Blue Sky Law that has historically been used in the prosecution and investigation of securities fraud. The Martin Act confers a variety of broad law enforcement and investigatory powers on the state Attorney General in situations

where the Attorney General believes that companies or individuals are defrauding or intending to defraud investors. N.Y. GEN BUS. LAW, Art 23-A, § 325.

Although most regulation of securities in the United States is carried out by the federal government, the Securities and Exchange Act of 1933 permits states to enact their own securities regulations. Most states have adopted their own laws to regulate securities and these laws are commonly referred to as Blue Sky Laws. Unlike the Blue Sky Laws of many other states, however, New York's law empowers the Attorney General to investigate and prosecute conduct that he believes may be detrimental to investors in the United States without showing proof that a defendant acted intentionally or with negligence. The Martin Act was largely unused during much of the 20th century. However, Cuomo's predecessor Elliot Spitzer and Manhattan District Attorney Robert Morgenthau began using the law more frequently to investigate and prosecute brokerage firms and their executives in the wake of the Enron accounting scandal.

In his subpoenas of the power generating companies, Cuomo relied on the investigatory powers provision of the Martin Act. This provision permits the Attorney General to issue subpoenas and "require such other data and information as he may deem relevant…and make such special and independent investigations as he may deem necessary" in connection with activities that the Attorney General believes are deceiving investors. N.Y. GEN BUS. LAW, Art 23-A, § 325. In its Sept. 14, 2007 letter to Xcel, the Attorney General's Office specifically cited the company's construction of a coal-fired electric plant that will generate 750 megawatts of electricity without carbon capture and sequestration technology. Xcel's public filings indicate that the company is constructing a new 750 megawatt coal plant in Pueblo, Colorado. The Attorney General's letter indicated that the increased financial, regulatory, and litigation risks that Xcel will face due to the construction of this plant and its operation of coal-fired plants had not been adequately disclosed to investors. "Selective disclosure of favorable information or omission of unfavorable information concerning climate change is misleading," the Attorney General's letter went on to say. "Xcel cannot excuse its failure to provide disclosure and analysis by claiming there is insufficient information concerning known climate conditions and uncertainties." Similarly, the Attorney General's Sept. 14, 2007 letter to Dynegy specifically cited the company's proposal to build eight new coal-fired power plants that would increase Dynegy's carbon dioxide emissions by 200 percent. The letter to Dynegy went on to state that Dynegy made "no attempt to evaluate or quantify the possible effects of future greenhouse gas regulations" in its 2007 filings with the SEC.

Cuomo's letters to Xcel and Dynegy indicated that the Attorney General was concerned about the companies' failures to disclose climate change risks to all investors, but also specifically noted that the New York State Common Retirement Fund was a "significant holder" of Xcel and Dynegy stock. Therefore, while Cuomo was exercising his broad Martin Act powers to protect all Xcel and Dynegy investors from what his office perceived to be deceptive activities by the companies, he was also acting on behalf of the state as manager of New York's pension fund.

Possible Precedent for Disclosure from Other Entities

The other power generating companies subpoenaed by the New York Attorney General's Office in 2007 were AES Corp., Dominion Resources Inc., and Peabody Energy Corp. When it announced the Xcel settlement, Cuomo's office indicated that negotiations were underway concerning settlements with the other companies.

Although the Attorney General's letters accompanying the subpoenas stated that Xcel and Dynegy made no disclosure on projected GHG emissions from their operations in their recent securities filings, power companies, including those subpoenaed by Cuomo, had been increasing their disclosure of the risks associated with climate change over the past few years prior to the issuance of the subpoenas. Xcel, for example, has provided information concerning the impact of climate change on its operations in its responses to the Carbon Disclosure Project questionnaires in 2006, 2007, and 2008. In its

responses, Xcel discussed the regulatory and physical risks it faces as a result of climate change, actions it is taking and planning to address those risks, and specifics on its carbon dioxide emissions. The Carbon Disclosure Project, on behalf of 475 institutional investors with a combined $55 trillion of assets under management, has been soliciting information from public companies concerning climate change risk since 2002. In connection with its most recent report, the Climate Disclosure Project issued a request to 3,000 of the largest companies in the world for information relating to risks and opportunities associated with climate change.

And although the Xcel and Dynegy settlements represent the first binding agreement between government and private industry regarding climate change disclosure, companies have recently been faced with increasing calls from private investors for better disclosure on this issue. Shareholder resolutions on climate change have increased significantly over the past few years: in 2004, twenty-five climate disclosure proxies were tendered to public companies. In 2008, at least fifty-seven such proxies were filed. An example of a climate disclosure proxy is the proxy filed by the New York City Pension Funds, Connecticut State Treasurer's Office, and Benedictine Sisters of Texas requesting reports from TXU Corp concerning that company's response to regulatory pressure to reduce GHG emissions. In September 2007, a coalition of environmentalists and institutional investors, organized by Ceres, with assets under management in excess of $1.5 trillion, petitioned the SEC to formally require the disclosure of climate change-related risks in connection with the filings of publicly traded companies. The disclosures agreed to in Xcel and Dynegy's settlements may prove to be a valuable precedent for companies looking to expand their climate change disclosure in the wake of these resolutions and petitions.

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ASTM ISSUES DRAFT STANDARD ON CLIMATE CHANGE DISCLOSURES

Lewis B. Jones

For those companies seeking guidance on climate change disclosures, ASTM International is preparing to answer the call. The voluntary standards organization, originally known as the American Society for Testing and Materials, published a draft standard for financial disclosures attributed to climate change on Nov. 19, 2008.

A Voluntary Standard, For Now . . .

Reporting entities should pay close attention to the new ASTM standard. On one hand, it purports to be voluntary: "This guide is intended for use on a voluntary basis by a reporting entity that provides disclosure in its financial statements regarding material financial impacts attributed to climate change. The degree and type of disclosure depends on the scope and objective of the financial statements." On the other hand, the drafters are well aware that many other ASTM standards have become mandatory after being adopted by other organizations, including regulatory agencies. Key elements of the standard could become incorporated into Financial Accounting Standards Board (FASB) disclosure standards or Securities Exchange Commission (SEC) rules. (For example, Section 12(d) of the National Technology Transfer and Advancement Act of 1995 specifically directs federal agencies "to use technical standards that are developed or adopted by voluntary consensus standards bodies," such as ASTM, "unless their use would be inconsistent with applicable law or otherwise impractical." 15 U.S.C. § 272 (note).) In addition, many companies routinely require suppliers and contractors to comply with all ASTM standards. And even if the standard remains purely voluntary, it might still become the industry standard—and hence a measuring stick against which to judge the adequacy of a given disclosure.

Principles

The draft standard states that ASTM does not intend to take a position concerning the science, anthropogenic contribution, future federal actions, or

other political aspects of climate change. Politics and science aside, the financial reality is that companies are already facing impacts attributed to climate change. ASTM is therefore responding to requests from numerous parties seeking additional guidance and a consistent structure for financial disclosures.

In a similar fashion, the draft standard states that reporting entities must separate their own positions with regard to the existence or extent of climate change from their assessment of financial impacts. Regardless of any position an entity might hold, "there remains uncertainty with regard to the final resolution of factual, scientific, technological, regulatory, and judicial matters, which could affect its impacts related to climate change." Therefore ASTM recommends the development of reasonable scenarios or ranges to recognize and address uncertainties.

The draft standard also recognizes that "appropriate disclosure does not necessarily mean exhaustive disclosure. There is a point of diminishing returns." The draft standard states, however, that "all relevant and reasonably ascertainable information should be used to determine the content of the disclosure."

Determining Whether Disclosure Is Warranted

The draft standard provides that disclosure should be made when an entity believes aggregate financial impacts attributed to climate change are material. Potential financial impacts include, but are not limited to, damages attributed to the entity's products or processes, regulatory compliance costs (including changes in resource costs, technology costs, and distribution and transportation costs), physical costs (including asset impairments), changes in income due to changes in markets, and litigation and management costs.

Once an entity has identified potential financial impacts, it should determine whether they (1) have a likelihood that is more than remote; (2) could have a severe impact that would disrupt the normal functioning of the entity or the entity's financial position, cash flows, or operations; or (3) are near-term, occurring during the next year. If any one of these criteria are met, the entity should estimate the likelihood, magnitude, and timing of the potential impact.

Content of the Disclosure

The draft standard proposes specific content for disclosures, as summarized below:

1. If applicable, identification of the company's historical (if possible, covering at least the last 5 years) and current total greenhouse gas emissions, including the methodology for calculating these data, the accounting year during which the measurements were made, whether there has been external verification or auditing of this data, an explanation of any major changes from historical levels, and, if available, projected ranges of future emissions.
2. A statement concerning management's strategic analysis of risks and opportunities related to climate change.
3. Identification of relevant state and federal regulatory requirements relating to climate change, with disclosure of the resulting financial impacts.
4. The estimated likelihood, magnitude, and timing of financial impacts attributed to climate change, along with a description of the approach used to quantify the impacts, a description of the method used to determine materiality, and for liabilities, the amounts accrued by the reporting entity.

These topics cover essentially the same ground, though in more detail, as the minimum disclosures required of Xcel Energy and Dynegy under recent Consent Decrees with the State of New York.

Process

The draft issued on Nov. 19, 2008 is the second subcommittee ballot for the draft standard. ASTM has encouraged wide distribution of this standard and is committed to reviewing all comments received. Although the comment period is now closed (as of Feb. 2, 2009), the standard will next move from the E50.05 Subcommittee on Environmental Risk Management to the full Committee on Environmental

Assessment, Risk Management and Corrective Action, where there will be another round of voting. The full committee will address all comments received. For more information contact Dan Smith at dsmith@astm.org.

Conclusion

This standard prepared by ASTM should provide much-needed guidance for reporting climate change disclosures. Once issued in final form, the standard is likely to be widely adopted. Therefore individuals with concerns about the content of climate change disclosures should take advantage of the opportunity to comment on the next draft.

Lewis Jones *practices environmental law at King & Spalding in Atlanta, Georgia. In addition to general environmental litigation, he counsels clients on issues related to climate change.*

MODERN DUE DILIGENCE: OPPORTUNITIES AND CHALLENGES IN THE GREEN ECONOMY

Mike Wallace
Michael Berg

If you are a legal advisor to corporations, you are likely on the receiving end of a growing pile of due diligence requests about your company's (or client's) *sustainability performance*. These requests may be initially sent to the CEO, CFO, Investor Relations Department, or the Environmental Health & Safety Department, but they typically work their way through the organization seeking a legal perspective—*To report or not report? That is but the question.*

Traditionally, companies have perceived voluntary sustainability and/or environmental disclosures as an unnecessary burden and risk. Today, however, growing demand from customers, consumers, employees, and investors has made these types of voluntary disclosures a necessity rather than an option.

Requests for sustainability information are increasing in both quantity and depth, and are coming from a growing number of stakeholders, including trillion dollar investor coalitions consisting of numerous mainstream investment firms. To many, requests to report on sustainability may seem like an unnecessary burden or a distraction from core business. These requests, however, should also be viewed as opportunities to access new capital and foster valuable business relationships.

Companies, both public and private, are becoming increasingly measured, evaluated, and ranked based on their ability to manage carbon and a series of other environmental and sustainability issues. From large retailers to mainstream investment firms, companies are being judged on a variety of sustainability criteria. This form of "modern due diligence" requires companies to produce some type of sustainability story. Alternatively, failure to provide sustainability and environmental information can send a negative message in several public arenas where companies are compared against their peers.

Market Demand for Sustainability Disclosure

Whether or not companies are voluntarily reporting about their own sustainability performance, enough information exists in the marketplace to enable interested stakeholders to extrapolate on sustainability performance. Within the U.S. Environmental Protection Agency databases alone, interested stakeholders can easily identify leaders on climate action on the same Web site as companies with long legacies of contaminated property.

Part of this shift is being driven by shareholder concerns about material risks and a growing interest in transparency, particularly on carbon risk management. In the United States, over a dozen public pension plans like CalPERS and CalSTRS—the two largest state employee pension funds in the United States—are coordinating their environmental efforts and using their combined influence to raise awareness on these issues. Some of their environmental actions are being coordinated by the Investor Network on Climate Risk

(INCR), which regularly produces reports that list and rank companies based on sustainability performance criteria. INCR is one of several trillion dollar shareholder coalitions focused on increasing corporate reporting on non-regulated, environmental performance issues.

The world's largest shareholder coalition on any single topic is the Carbon Disclosure Project (CDP), which has been around for over eight years. At last count, the CDP consisted of over 475 institutional investors representing more than $55 trillion dollars of investment capital. The CDP solicits carbon emissions information from the world's largest publicly traded corporations and serves as a public repository for this information. Its annual survey is submitted to over 3,000 companies and responses are posted on its Web site. The CDP, through a variety of intermediaries, also produces annual reports that detail best and worst practices in transparency and reporting.

Over the past year, we've seen investor coalitions increasingly focus on issues beyond carbon risk and more actively push for sustainability disclosure. In December 2008, a trillion-dollar investor coalition requested that the CEOs of 100 major corporations sign on to its Water Mandate. In October 2008, 9,000 CEOs received letters from the United Nations Principles for Responsible Investment (UN PRI), another trillion-dollar investor coalition, requesting that they either sign on to UN PRI's broad sustainability principles or explain in writing why they have elected not to do so. Also in 2008, investor coalitions filed over 300 sustainability-oriented shareholder resolutions. The resolutions included requests that companies engage in greater sustainability disclosure, as well as a number of other sustainability-related requests.

In addition to the market push for voluntary reporting, companies may soon face increased regulatory demands for sustainability reporting. For example, the upcoming 2010 UK Carbon Reduction Commitment is projected to require roughly 5,000 companies to measure and report carbon dioxide emissions under a new cap-and-trade regime. While U.S. companies, both public and private, may think that this does not apply to them, remember the other supply chain ripples we have all experienced—ISO9000, Y2K, and ISO14000. A carbon footprint is influenced by the supply chain and companies are increasingly asking their suppliers to measure and report on carbon emissions.

Increased Reporting = Increased Transparency

As the number of companies that report on sustainability performance grows, the depth of reporting and the demand for transparency and verification has grown. Many companies are now proactively collecting and posting their sustainability performance reports online in the form of annual Sustainability Reports. According to a 2008 KPMG study, nearly 80 percent of the 250 largest companies have issued Sustainability Reports—a 50 percent increase from 2005. This type of information is aggregated, analyzed, and stored on numerous public Web sites, which enable shareholders, employees, customers, and other stakeholders to quickly see who is and isn't reporting.

In 2008, 688 companies registered their reports with the Global Reporting Initiative (GRI), the leading standard for sustainability reporting. The GRI calls for a detailed reporting framework and "grades" reports based on the level of disclosure. As with financial reporting, there is a push for sustainability report data to be verified or assured by a third party. According to a report from CorporateRegister.com, over 650 assurance reports were produced in 2007, and the number has grown 20 percent each year over the past decade.

Cause or Effect

The rise in environmental disclosure and sustainability reporting is the result of a delicate balance between interested stakeholders and their companies. As one would expect, stakeholders and companies contradict one another on the "cause and/or effect" of their respective actions. Nonetheless, the proliferation of sustainability performance data has created an atmosphere of expansion in which both stakeholders and companies are using sustainability reporting to advance their respective interests. Thus, the pressure

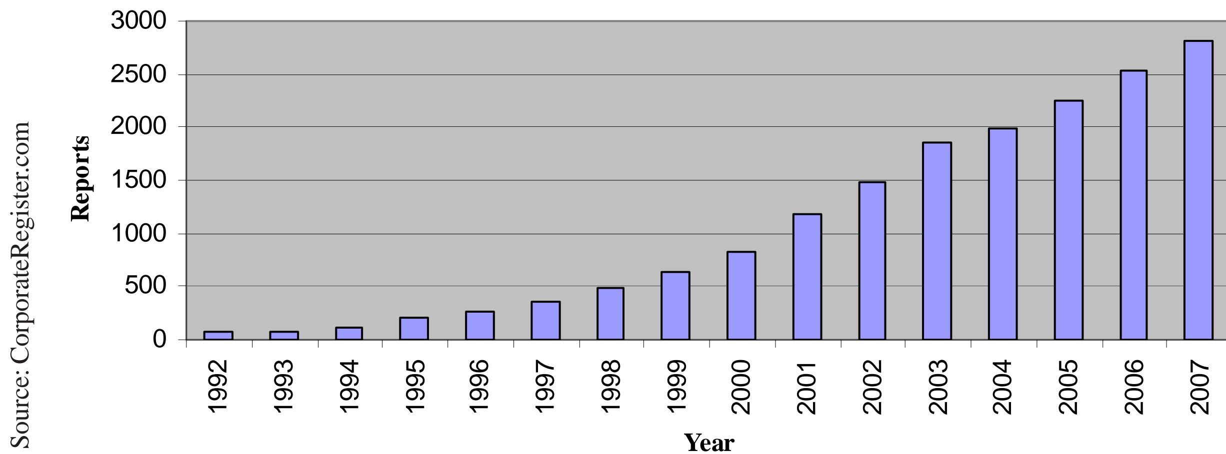

Figure 1. Corporate Register: Number of Reports (1992-2007)

from stakeholders and the number of reporting companies will continue to ebb and flow. See Figure 1.

From Burden to Opportunity

The process of collecting and reporting sustainability data, while initially burdensome, generally presents a host of advantages and opportunities—namely access to new capital, reputational enhancement, and the identification of operational efficiencies. Both public and private companies are experiencing the need to address the sustainability question to gain access to customers, investment capital, and public grant monies, and to retain and attract human capital.

Without understanding, collecting, measuring, and reporting, it is impossible to effectively communicate with interested audiences. Additionally, the process of collecting environmental data, such as a firm's carbon or water footprint, often reveals opportunities for companies to identify potential cost savings.

Access to Investment Capital

Companies who report transparently on sustainability performance can enhance their access to capital. Inclusion in sustainability-oriented indices like the Dow Jones Sustainability Index (DJSI) and the FTSE4Good is a common goal of companies looking for recognition in this space; these indices are also a useful screen for investors seeking sustainable companies. In the last few years, the number of sustainability-oriented investment products coming from mainstream institutions has increased rapidly. A 2007 report from TIAA-CREF stated that $2.7 trillion—approximately 11 percent of all U.S. assets under professional management (nearly one out of every nine dollars)—is being invested in companies that use sustainability performance criteria. These investors are actively searching and analyzing companies to find those with the most credible sustainability data.

Access to Public Monies

In addition, governors, mayors, and national officials are increasingly offering a variety of resources and financial incentives for implementing "clean" (another name for "sustainable") technologies and solutions. Also, with the recent adoption of the Climate Principles for the finance industry by several large banks and insurers, lending and insurance will become increasingly tied to and incentivized by the sustainability reporting of clients and prospective clients. While this may not be "public" disclosure, it still requires companies to think about, gather, and report their sustainability performance.

Access to Human Capital

Companies are also finding that their sustainability reports can help attract and retain human capital. For example, several well known annual lists highlight companies based on sustainability performance. Such lists include Fortune's Most Admired Companies, Innovest's 100 Most Sustainable Companies, and The CRO's Best Corporate Citizens. These lists, primarily based on the analysis of publicly available sustainability data, play a growing role in attracting and retaining top talent. A recent Cone study found that 77 percent of Americans consider a company's commitment to social issues when deciding where to work, up from 48 percent in 2001.

How can any of these stakeholders know the real and accurate story unless companies actively engage in the measurement of, management of, and some level of reporting on key sustainability indicators?

Comparability

The growing interest in sustainability in all sectors of the economy has created a unique collection of publicly available information and data resources. This information is now easily accessible and actively used by investors, research firms, customers, consumers, prospective employees, journalists, and activist organizations. Mainstream investors and specialized research providers, in particular, are becoming increasingly interested in how companies are managing carbon and other sustainability issues. As the breadth and depth of sustainability reporting grows, the sustainability bar is raised and non-reporting companies are becoming viewed with greater scrutiny. Given the current stakeholder focus on quantifiable performance metrics like carbon emissions and water use, reporting on these types of indicators is most critical. As more and more companies are reporting sustainability performance in quantitative terms, influential stakeholders can now easily compare and contrast data across entire sectors. For example, someone who is interested in your industry can view the Carbon Disclosure Project's annual Global 500 report and see your company measured against your peers. They can also see whether your company decided not to respond or chose not to make your response available to the public. See Figure 2.

The Need to Respond

If you are the only company in your industry that isn't reporting sustainability performance in quantified terms, what messages are you sending to interested and influential stakeholders? If you are being asked directly and repeatedly by shareholders about your sustainability performance and you are not responding, what message are you conveying?

- Your questions aren't important
- You're not important
- We don't have time to deal with such issues
- We can't deal with such issues
- These issues aren't relevant to our industry
- Even though a majority of our peers are measuring and reporting, these issues are not important to us

What if your largest customer asks all its suppliers to report sustainability information? If you are the only supplier unable to supply relevant and verifiable data, what will your customer think?

Aligning Sustainability with Corporate Governance

Sustainability disclosure now has a direct link to corporate governance in that shareholders are asking for greater transparency, seeking quantifiable environmental data, and actively using sustainability performance data as a proxy for assessing overall corporate governance. Companies who ignore these requests raise greater issues about the overall quality of the governance of their organization.

We recommend that companies engage in what we refer to as "environmental governance"—leveraging existing corporate governance systems to measure, manage, and then respond to the growing market demands for sustainability information while capitalizing on the numerous strategic disclosure opportunities. Companies who engage in active environmental governance will be rewarded in the marketplace.

CDLI scores and emissions disclosure for all respondents, by sector
Chemicals & Pharmaceuticals Sector

Company	CDLI score	Scope 1*	Scope 2*	Scope 3**	Intensity***	CDP5	CDP4
Abbott Laboratories	52	890	814	0	66	AQ	AQ
Air Liquide	30	8,100	7,995	442	863	AQ	AQ
Air Products & Chemicals	54	13,000	9,000	–	2,192	AQ	AQ
Akzo Nobel	45	800	2,400	–	198	AQ	X
Alcon – See Nestle	–	–	–	–	–	AQ	AQ
Allergan	63	41	78	–	30	AQ	AQ
Amgen	38 (NP)	–	–	–	–	AQ	AQ
Astellas Pharma	41 (NP)	–	–	–	–	AQ	AQ
AstraZeneca	73	442	276	576	24	AQ	AQ
BASF	82	23,463	4,050	28,190	346	AQ	AQ
Baxter International	74	252	476	162	65	AQ	AQ
Bayer	78	3,890	3,710	-69,800	171	AQ	AQ
Becton Dickinson & Co.	39	72	408	–	75	AQ	AQ
Bristol-Myers Squibb	64	435	537	54	50	AQ	AQ
Celgene Corporation	DP	–	–	–	–	DP	X
Covidien	DP	–	–	–	–	X	X
Daiichi Sankyo	46 (NP)	–	–	–	–	AQ	AQ
Dow Chemical Company	66	29,600	7,700	–	691	AQ	AQ
E.I. du Pont de Nemours & Company	63	9,800	4,200	–	476	AQ	AQ
Eli Lilly and Company	53	614	1,457	106	111	AQ	AQ
Formosa Petrochemical	NR	–	–	–	–	NR	NR
Genentech	62	42	78	31	13	AQ	IN
Genzyme Corporation	35 (NP)	–	–	–	–	AQ	AQ
Gilead Sciences	2	–	–	–	–	AQ	AQ
GlaxoSmithKline	62	872	1,095	3,832	43	AQ	AQ
Johnson & Johnson	74	343	580	244	15	AQ	AQ
Medtronic	36 (NP)	–	–	–	–	AQ	AQ
Merck & Co.	58	779	583	–	56	AQ	AQ
Monsanto Company	41	1,305	840	67	251	AQ	IN
Mosaic Company	NR	–	–	–	–	X	X
Novartis	69	586	883	146	39	AQ	AQ
Novo Nordisk	56	204	32	–	28	AQ	AQ
Pfizer	67	1,058	1,136	–	45	AQ	AQ
Potash Corporation of Saskatchewan	54	9,000	3,300	–	2,350	AQ	AQ
Praxair	74	3,168	11,000	260	1,507	AQ	AQ
Roche Holding	42	439	496	109	24	AQ	AQ
Sanofi-Aventis	52 (NP)	–	–	–	–	AQ	AQ
Schering-Plough	61	140	419	131	44	AQ	AQ
Shin Etsu Chemical	37 (NP)	–	–	–	–	AQ	AQ
Stryker Corporation	NR	–	–	–	–	DP	AQ
Syngenta International	51 (NP)	–	–	–	–	AQ	X
Takeda Pharmaceutical	NR	–	–	–	–	AQ	AQ
Teva Pharmaceutical Industries	NR	–	–	–	–	NR	NR
Wyeth	49	551	602	–	51	AQ	AQ

Source: CDProject.net

Figure 2. 2008 CDP: Responses for Chemicals & Pharmaceuticals Sector

First, companies should conduct internal and external reviews to see what information exists, determine what to report, and identify to whom they should report. It is crucial to know what is being reported by your company, through which departments, and to what level of detail and accuracy. Whether you realize it or not, your company is probably collecting and reporting some form of sustainability information to local, state, and federal agencies.

Second, understand your external stakeholders, their interests, and their information sources. This is key in preparing for the onslaught of sustainability questions. The challenge for most businesses is identifying the most important stakeholders, responding to the highest priority (i.e., material) concerns while developing constructive communication channels. These stakeholders can contribute positively to corporate decision-making by providing an external perspective and acting as external eyes and ears on emerging sustainability issues.

Third, companies should then begin reporting. It is vital, however, to coordinate these disclosures. In essence, all these pieces of information create a sustainability story whether or not your company is actively producing one. It is therefore essential to review operations and management systems through a sustainability lens.

Lastly, companies need to actively manage the information that is being reported about them. In particular, companies should be aware of:

1. Any sustainability performance information that is being publicly released;
2. How your company is being listed, ranked, and rated, and whether these methods are accurate and reliable;
3. Who internally receives and responds to requests for information about your company; and
4. Whether policies and procedures are in place to ensure that sustainability performance information leaving the company is reliable and accurate.

For example, we recently worked with a large biotechnology firm who had been producing sustainability reports for a number of years but had been ignoring the specific requests sitting in the inbox of Investor Relations. This exposed them to added scrutiny in their industry and excluded them from opportunities for access to investment capital. We connected Investor Relations with corporate counsel and EH&S and identified voluntary reporting opportunities. The firm began by responding to some of the high priority requests and then expanded their voluntary efforts. They are now a part of the Dow Jones Sustainability Index, as well as several other voluntary initiatives that publicly report this company's leadership in the area of sustainability. With minimal effort, this organization is now demonstrating leadership in the area of sustainability, has identified and reported on cost and waste reductions, and has opened up new opportunities to attract investment, talent, and customers.

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