



Investor Environmental Health Network

HEALTHY PEOPLE...HEALTHY BUSINESS

July 15, 2016

Brent J. Fields
Secretary
Securities and Exchange Commission
100 F Street, NE,
Washington, DC 20549-1090

Via email to rule-comments@sec.gov

Re: File Number S7-06-16 - Regulation S-K Concept Release on Business and Financial Disclosure Required by Regulation S-K

Dear Mr. Fields:

I am writing on behalf of the Investor Environmental Health Network (IEHN) to comment on the Regulation S-K Concept Release. Our comments focus on sustainability disclosure, materiality, and prescriptive and principled disclosure models. We include specific recommendations for SEC guidance and regulations to address shortcomings in the current Regulation S-K disclosure framework.

In order of this letter we address Concept Release questions 6, 216, 219, 217 and 14.

About the Investor Environmental Health Network

IEHN is a collaborative partnership of investment managers (\$50B AUM) concerned with financial and public health risks associated with corporate toxic chemicals policies. Engaging through dialogue and shareholder resolutions, IEHN members¹ encourage companies to adopt policies to continually and systematically reduce and eliminate the toxic chemicals in their products and activities. Recent focus issues for our investor members have included risks and opportunities associated with toxic materials in products including pesticides, cosmetics and household cleaners, the environmental impacts of hydraulic fracturing, and linking executive compensation to sustainability metrics.

¹ Members of IEHN include Adrian Dominican Sisters, As You Sow Foundation, Basilian Fathers of Toronto, Bon Secours Health System, Inc., Boston Common Asset Management, LLC, Calvert Group, LTD, Dignity Health, Domini Social Investments, LLC, First Affirmative Financial Network, LLC, Green Century Capital Management, Inc., Harrington Investments, Inhance Investment Management, Inc., Maryknoll Sisters, Mercy Investment Program, Miller/Howard Investments, Inc., Newground Social Investment, Parnassus Investments, Pax World Funds, Portfolio 21, Sisters of Mercy, Regional Community of Detroit, Sisters of St Francis of Philadelphia, Trillium Asset Management Corporation, and Trinity Health.

Key Interests of IEHN Members Regarding Disclosure

Of key interest to our organization and investor members are the risks and benefits of management of potentially harmful chemicals utilized in products, services and activities of registrants. Our members focus on the potential positive and negative financial impacts on individual portfolio companies, and also on reducing the economic and public health impacts on society. Many companies that our members are monitoring and engaging with are systematically working to eliminate chemicals of concern to consumers and the scientific community.

Some leading companies such as Walmart, CVS Health, Nike, Apple, and HP have established extensive programs and processes to eliminate a targeted group of chemicals of concern from use in their products or services. This systematic approach is seen as an opportunity to elevate corporate reputations, boost consumer confidence and reduce liabilities.

SUMMARY OF RECOMMENDATIONS

Require enforceable, prescriptive, line item disclosures for sustainability including links to external sustainability reporting.

Require environmental penalty amount disclosures (\$100,000 threshold) to include disclosure of penalties AFTER assessed as well as when anticipated.

Establish more prescriptive guidance for disclosure of emerging science and risks.

Even though financial impact on value varies from sector to sector, line item disclosures on sustainability are advisable and will remain material.

Require a statement of significant audiences and materiality.

ANALYSIS

I. Discussion of Concept Release Questions 6 and 216

Concept Release Question 6.
Prescriptive or Principles-Based Approaches

6. Should we limit prescriptive disclosure requirements and emphasize a principles-based approach? If so, how? How can we most effectively balance the benefits of a principles-based approach while preserving the benefits of prescriptive requirements?

Concept Release Question Number 216.
What Sustainability or Public Policy Issues Are Important to Investors?

216. Are there specific sustainability or public policy issues important to informed voting and investment decisions? If so, what are they? If we were to adopt specific disclosure requirements involving sustainability or public policy issues, how could our rules elicit meaningful disclosure on such issues? How could we create a disclosure framework that would be flexible enough to address such issues as they evolve over time? Alternatively, what additional Commission or staff guidance, if any, would be necessary to elicit meaningful disclosure on such issues?

A. Prescriptive requirements may ease the process of enforcing against materially misleading statements and omissions

As investors focused on specific sustainability issues, we seek reliable disclosure of metrics related to those issues, as well as management's discussion of its response strategies.

At present, most such disclosures occur in voluntary frameworks such as Corporate Social Responsibility reports. These voluntary reporting frameworks are notorious for the tendency of reporting companies to highlight the “good” news but omit negative developments. Because such reports are intended for and utilized by investors, we believe that the protections of the securities laws against materially misleading statements and omissions are applicable to those reports. However, we are aware that the Commission and its staff currently are not substantially attentive to the content of such reports.

Establishing a mandatory disclosure framework as part of the securities laws would be one possible strategy for exposing a smaller amount of data to the anti-fraud scrutiny provided for securities filings. However, we believe that securities regulators and investors should deploy all available authority and influence to prevent materially misleading or incomplete disclosures in CSR reports and other voluntary corporate disclosures.

The SEC has authority to act in this area both through scrutiny of the existing CSR reports, and through disclosure rules which effectively embrace (and advise companies) that CSR

information is relevant to SEC and investor enforcement actions pursuant to the antifraud Rules 10b-5 and 14a-9.²

As we suggest below, in addition to any other line items or requirements on sustainability reporting the Commission adopts, securities filings should be required to state which sustainability reporting standards and frameworks a company utilizes, and to provide URL links and page references regarding how to access the related documents.

Recommendation: Establish enforceable, prescriptive, line item disclosures for sustainability and links to external sustainability reporting

The Securities and Exchange Commission can go further to prevent misleading statements and omissions on sustainability matters by (1) prescriptive requirements for sustainability disclosure for which accuracy and completeness are easily ascertained and (2) the use of administrative enforcement mechanisms to address violations without a need to demonstrate a “knowing” misleading statement or omission or to document the financial impact on the investors.³

It is essential to modernize US securities laws to make it less attractive for companies to engage in misleading communications about environmental benefits or impacts of their activities, and to ensure that all voluntary reporting intended to reach investors and their analysts is conducted in contemplation of the securities law requirements that prohibit materially misleading investors. Increasing the reliability and completeness of CSR reporting should be part of the overall SEC strategy on sustainability disclosure.

² Rule 10b-5 states “It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange... (b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or ... in connection with the purchase or sale of any security.” Rule 14a-9 states, “No solicitation subject to this regulation shall be made by means of any proxy statement, form of proxy, notice of meeting or other communication, written or oral, containing any statement which, at the time and in the light of the circumstances under which it is made, is false or misleading with respect to any material fact, or which omits to state any material fact necessary in order to make the statements therein not false or misleading or necessary to correct any statement in any earlier communication with respect to the solicitation of a proxy for the same meeting or subject matter which has become false or misleading.”

³ See Rachel Cherington, Securities Laws and Corporate Social Responsibility: Toward an Expanded Use of Rule 10B-5, 25 J. Int'l L. 1439 (). Available at: <http://scholarship.law.upenn.edu/jil/vol25/iss4/5>; Cadesby B. Cooper, Rule 10b-5 at the Intersection of Greenwash and Green Investment: e Problem of Economic Loss, 42 B.C. Env'tl. A . L. Rev. 405 (2015), <http://lawdigitalcommons.bc.edu/ealr/vol42/iss2/5>

B. The Commission should retain the prescriptive disclosure of Item 103 instruction 5C, (disclosing anticipated environmental penalties in excess of \$100,000) but refine the provision to make it enforceable.

The Concept Release notes that Item 103 note 5C is under current consideration for revision. This is the requirement to disclose pending environmental proceedings which could result in penalties in excess of \$100,000.⁴

This provision has proven a notorious point of noncompliance. Studies in 1998 and 2009 confirmed that most registrants were not complying.⁵ As noted in the studies, the lack of effective enforcement of the requirement leads to this widespread noncompliance. The \$100,000 anticipated penalties provision is a valid provision, but it will only be widely complied with when accountability is built in. The SEC and investors must be able to review these penalty trends both as anticipatory penalties, but also as to the amount of penalties actually assessed.

Recommendation: Require environmental penalty amount disclosures to include disclosure of penalties AFTER assessed as well as anticipated

We recommend that \$100,000 figure be retained, but registrants be required to disclose not only anticipated penalties, but also the amount of penalties after finalized. By requiring disclosure retroactively as well as prospectively under this provision, the Commission would be better positioned to enforce the anticipatory requirement, by being enabled to routinely scrutinize the failure of anticipatory disclosures. Without this additional disclosure, there is little accountability of individual companies – investors are not informed of penalties in excess of \$100,000 actually received, are not informed of prospective proceedings, and the rule is nearly unenforceable.

**II. Response to SEC Concept Release Question Number 219
Which Reporting Frameworks Are Appropriate Sources For Line Item Disclosure?**

219. In an effort to coordinate ESG disclosures, several organizations have published or are working on sustainability reporting frameworks. Currently, some registrants use these frameworks and provide voluntary ESG disclosures. If we propose line-item disclosure requirements on

⁴ Item 103: Material Pending Legal Proceedings: “Describe briefly any material pending legal proceedings, other than ordinary routine litigation incidental to the business, to which the registrant or any of its subsidiaries is a party or of which any of their property is the subject... Instruction 5:

“[n]otwithstanding the foregoing, an administrative or judicial proceeding (including, for purposes of A and B of this Instruction, proceedings which present in large degree the same issues) arising under any Federal, State or local provisions that have been enacted or adopted regulating the discharge of materials into the environment or primary [sic] for the purpose of protecting the environment shall not be deemed ‘ordinary routine litigation incidental to the business’ and shall be described if: ... C. A governmental authority is a party to such proceeding and such proceeding involves potential monetary sanctions, unless the registrant reasonably believes that such proceeding will result in no monetary sanctions, or in monetary sanctions, exclusive of interest and costs, of less than \$100,000; provided, however, that such proceedings which are similar in nature may be grouped and described generically.”

⁵ See for instance <http://www.csmonitor.com/Environment/Bright-Green/2009/0224/study-most-companies-lie-to-sec-about-environmental-fines>

sustainability or public policy issues, which, if any, of these frameworks should we consider in developing any additional disclosure requirements?

A. The Securities and Exchange Commission should encourage registrants to integrate, identify and cross-reference voluntary disclosure guidelines and key performance indicators utilized on sustainability issues.

Regulation S-K promotes the use of key performance indicators in disclosure reports. Registrants should be encouraged to utilize, integrate and reference sustainability performance indicators relevant to their operations.

As an investor coalition which has long participated in voluntary standard-setting organizations and processes, we are well aware of the strengths and weaknesses of various of the voluntary standards in this field. However, we believe that it is far more important to inform investors regarding which disclosure frameworks the firm is utilizing than to select a single standard for adoption at the SEC.

Although there are obvious market leaders on sustainability disclosure (SASB, GRI, CDP and UNPRI, for instance) many other disclosure standards set by investor coalitions and NGOs on issues such as human rights, hydraulic fracturing practices, deforestation, responsible sourcing, executive compensation, etc. are also relevant.

We do not recommend that the SEC take action that would preempt or prefer one set of these standards over another. Instead, we suggest that SEC guidance or rules should encourage companies to disclose all reference standards or programs utilized on issues of sustainability with either direct integration to the MD&A of the relevant disclosures, or at a minimum, URL links that allow investors to access the related materials.

One mechanism for doing so would be to utilize an index such as the GRI index to list sustainability issues and for the company to provide next to each line item the standards utilized for disclosure and a link, when available, to disclosures by the company regarding each indexed issue. For instance, a listing on a product toxicity index item might state:

"Disclosure pursuant to GRI (or SASB) standards; 2016 CSR report [URL] page 25."

Example: hydraulic fracturing disclosure standards

On the issues on which the Investor Environmental Health Network members engage companies, there are numerous examples of disclosure benchmark documents developed by trade associations, NGO-company partnerships, investor organizations and accounting organizations.

In 2011, to clearly articulate investors' reporting expectations, the Investor Environmental Health Network ("IEHN") and the Interfaith Center on Corporate Responsibility ("ICCR") published Extracting the Facts: An Investor Guide to Disclosing Risks from Hydraulic Fracturing

Operations.⁶ An eighteen-month investor dialogue with energy companies, convened by Boston Common Asset Management and Apache Corporation, and supported by members of ICCR and Ceres, provided a venue for extended conversations concerning risks, management practices, and disclosures associated with hydraulic fracturing operations and a forum for industry experts to review draft practices and indicators. The dialogue became the foundation for Extracting the Facts. The report identifies 12 core management goals, best management practices, and key performance indicators on which investors require disclosure to adequately assess risk management practices. Extracting the Facts was intended to promote a “race to the top,” encouraging companies to be more transparent and strive for and report on best practices. The guidelines focus on encouraging companies to implement best management practices or to explain why such practices cannot be carried out.

Extracting the Facts has been widely referenced and utilized by investors. Investors on three continents (Australia, Europe, and North America) managing more than \$1.3 trillion in assets have expressed support for the guidelines. The guidelines have also been used as the basis for internal risk evaluations conducted by JPMorgan Chase, reportedly the largest energy lender in the United States, and by Standard Chartered and Credit Agricole.⁷ The guidelines have also drawn support from companies and nongovernmental advocacy organizations.

Our members and other investors have also used the framework to benchmark companies. Disclosing the Facts: Transparency and Risk in Hydraulic Fracturing Operations is an annual review that benchmarks 30 oil and gas companies on their disclosures against the performance indicators across five areas of environmental, social, and governance metrics: (1) Toxic chemicals; (2) Water management: sourcing, well integrity, waste management, and water quality monitoring; (3) Air emissions; (4) Community impacts; and (5) Management and accountability.

The companies reference these guidelines in shaping their disclosures and sometimes specifically reference the guidelines themselves. Referring to the investor disclosure scorecard report based on Extracting the Facts, BHP Billiton has stated “The investor scorecard report issued last year gave a clear signal of where investors are seeking broader disclosure. We used that to help improve our public reporting this year.”⁸

⁶ <http://iehn.org/documents/frackguidance.pdf>

⁷ See page 53 at http://www.jpmorganchase.com/corporate/Corporate-Responsibility/document/JPMC_Full_CR_Report_2013.pdf. See also, <http://iehn.org/documents/CPFIShaleGasGuidanceNoteApril2013.pdf>.

⁸ <http://www.mysanantonio.com/opinion/editorials/article/Disclosure-about-fracking-risks-best-policy-5974299.php>
Other companies shared these investor assessments on their websites and in their voluntary reports. For instance, Apache reports on its website:

Apache’s progress toward more environmentally friendly hydraulic fracturing was recognized in a report published by environmental stakeholders from As You Sow, Boston Common Asset Management, Green Century Capital Management and the Investor Environmental Health Network. Apache’s increased its overall score in 2014 and continues to be classified as one of the highest performing companies on a scorecard that ranked companies on disclosure of chemical use, water and waste management, air emissions, community impacts and management accountability.

In 2015, IEHN, with As You Sow and Boston Common Asset Management, published our third annual scorecard rating oil and gas companies' disclosures about their use of best practices. The report showed a dramatic improvement in company scores, with one company, BHP-Billiton, scoring at the 85th percentile. BHP wrote its fracking case study to the outline of Disclosing the Facts, providing a concise disclosure that places key information in one location and which can serve as a model for other companies.

Another eight companies comprise a core of leadership companies outpacing the rest of the industry on disclosure. Hess, Apache, Noble Energy, CONSOL Energy, Southwestern Energy, Anadarko Petroleum, QEP Resources and EQT. Some of these led in 2014 and increased their scores slightly, while several followed BHP's path, leaping from near the bottom of the 2014 rankings to be among the leaders. This group of companies trailing BHP mainly clustered around the 50% percentile, so they still have far to go.

Anadarko was so pleased with its improvement that in its inaugural sustainability report in early 2016, it devoted a full page to the scorecard, displaying all 30 companies' rankings.⁹

The other 70% of the 30 companies scored still leave investors substantially in the dark about their policies, practices, and impacts, especially on a quantitative play-by-play basis. This pattern mirrors that of most economic sectors, which evidence a wide spread between corporate leaders and laggards on environmental, social and governance matters.

Example: Chemical Footprint Metrics

One of the most leading developments for disclosure regarding chemical toxicity is the establishment of the Chemical Footprint Project (CFP). CFP provides a metric for benchmarking companies across multiple sectors as they select safer alternatives and reduce their use of

Anadarko reported in its CSR report:

"Disclosing the Facts" is a report issued every year by As You Sow, Boston Common Asset Management and the Investor Environmental Health Network (IEHN). This report is a scorecard of the 30 largest oil and natural gas companies engaged in hydraulic fracturing in the United States. The group issuing the report claims it "gauges how well the ... companies do in providing information so that investors can accurately assess how, or whether, these companies manage key risks of fracking..."

In 2015, the report recognized eight companies, including Anadarko, in making "substantial progress" in disclosures. The Company nearly doubled its score and moved from being tied for the 12th spot to being tied for seventh, with the score going from eight points to 15 points. Anadarko's approach in increasing transparency is to focus on what adds value to its shareholders.

9

chemicals of high concern. The Chemical Footprint Project, modeled on the Carbon Disclosure Project, measures overall corporate chemicals management performance by evaluating:

- Management Strategy
- Chemical Inventory
- Footprint Measurement
- Public Disclosure and Verification

The chemical footprint approach has drawn support from some large companies. In 2015, Becton Dickinson and Co., Clorox Company, and Johnson & Johnson, among others, participated in the Chemical Footprint Project survey. HP has announced in its CSR report that it will follow the model developed by CFP:

HP recognizes the importance of measuring substances of concern in our products and setting goals for improvement, so in 2016 we will formally participate in the Chemical Footprint Project (CFP). In 2013 and 2014, Hewlett-Packard Company helped develop and pilot the CFP, a third-party benchmark tool launched by Clean Production Action, the Lowell Center for Sustainable Production, and Pure Strategies, that provides companies with a standard way to evaluate progress toward reducing chemicals of high concern and to identify opportunities in this area

Finding safer alternatives

HP proactively evaluates materials in our products and supply chain, taking into account published lists of substances of concern, new and upcoming legal requirements, and customer preferences, as well as scientific analysis that reveals a potential impact to human health or the environment. When replacing substances of concern, we provide guidance to suppliers on commercially viable alternatives with lower potential impact.¹⁰

In addition, Walmart in announcing its recent success in eliminating 95% of 10 targeted substances noted that it was utilizing a “chemical footprint” approach to chemicals. It is clear the chemical footprinting approach applicable to a wide array of sectors will become an important metric for companies to report on. Ultimately, these metrics should find their way into SEC disclosure.

We believe this demonstrates the need for SEC disclosure rules on sustainability to have the flexibility to adapt to emerging metrics, standards and programs that an individual company is utilizing and to encourage inclusion of the relevant metrics and reporting in securities filings.

¹⁰ HP CSR Report, <http://h20195.www2.hp.com/V2/GetDocument.aspx?docname=c05154920>, pp. 46-47.

Need to improve principled AND prescriptive rules on disclosure of emerging issues such as emerging science and shifting demand by customers.

A litmus test for companies that we engage with on these issues is the degree to which a registrant takes a precautionary approach to management of chemical safety and toxicity concerns of consumers and scientific analysts.

Many chemicals of serious public health concern to the scientific community have not yet been restricted by regulatory bodies. For instance, there is a large body of evidence supporting concern about the effect of even low levels of exposure to certain compounds believed to disrupt the endocrine system, for example, and to pose developmental risks to vulnerable populations, especially developing fetuses and neonates.

Despite the lack of restrictions on various chemicals of concern to public health experts and consumers, many companies exercise a compliance mentality when it comes to chemical management, i.e. if government regulations do not prohibit inclusion of a chemical in a product, then it is considered acceptable for inclusion. This often places companies at risk of market lockouts, consumer exodus and liability.

Other companies and consumers have adopted a precautionary approach - not waiting for regulators to ban the materials in order to restrict their uses in certain products and services.

To cite one example, the British company Boots Group began phasing out polyvinylchloride (PVC) plastic from its cosmetic and toiletry products in 2008. Boots's actions implement the precautionary chemicals approach it adopted in 2003: "Where there are reasonable grounds for concern that a chemical used in our product could be harmful to human health or the environment, we will always take appropriate precautionary measures."

Boots, a UK company, merged with a Europe-based company named Alliance Unichem. They became Alliance Boots. Then Walgreens merged with the combined company and they became Walgreens Boots Alliance. The company has since then announced that the new "Walgreens Boots Alliance" will adopt the more stringent precautionary practices of Boots going forward. This is a highly material development from the standpoint of investors concerned with the quality of management of these issues.¹¹

These positive actions by these companies, however, stand in contrast to market laggards which are exposed to greater levels of reputational risk and liabilities due to their continued use of problematic materials and lack of a systematic elimination strategy. Consider these examples of investment impact cited in *Investing for a Sustainable Future*, MIT Sloan Management Review, Findings from the 2016 Sustainability Global Executive Study and Research Project:

Mismanaging a sustainability issue can also send investors running. In 2007, after

¹¹ CVS Health and WBA race to Rx for safer chemicals, Richard Liroff, <https://www.greenbiz.com/article/cvs-health-and-wba-race-rx-safer-chemicals>

lead paint was found in toys it manufactured in China, Mattel Inc. had to recall more than 20 million products. To help stem declines in the company's stock price and help its relations with China, Thomas A. Debrowski, Mattel's executive vice president for worldwide operations, publicly apologized to everyone affected by the recall, including the Chinese people. China was by no means a new market for Mattel. It had been doing business there since 1959, and was known for scrutinizing its manufacturing partners. But in this case, their efforts fell drastically short.

More recently, Lumber Liquidators Inc., based in Yonkers, New York, one of the largest and fastest-growing flooring retailers in North America, found itself on CBS's *60 Minutes* and the target of short sellers banking on the fallout of a sustainability fiasco. Lumber Liquidators sells hardwood and laminate flooring that is manufactured in China. The company allegedly fell significantly short of U.S. health and safety standards governing the amount of formaldehyde that can be used in products, putting thousands of people at heightened risk of respiratory irritation, asthma, and cancer.

Lumber Liquidators had once been a darling of investors. Its stock price rose from \$13 per share in 2011 to \$119 per share in 2013. In November 2015, a few months after the *60 Minutes* report aired, the share price plunged to less than \$15.

Another example of proactive responses involves the oil and gas exploration and production industry, reporting progress in reducing the toxicity of the fluids used in hydraulic fracturing operations. Companies are reporting less use of some of the more toxic individual chemicals in fracturing fluid mixtures and are setting up tracking systems for enhancing future reporting on the overall toxicity of their chemical mixtures. Companies are also collaborating with the American Chemical Society's Green Chemistry Institute to advance green chemistry in hydraulic fracturing. Such forward movement reflects both enhanced efforts by companies recognizing the business rewards of reducing highly controversial chemical risks and pressure from investors for companies to be more public about their risk-reduction efforts. The benefits from smarter management of chemicals include lower costs when fewer chemicals are used, reduced environmental damage from operating errors and accidents and reduced regulatory and litigation risk.¹²

Regulatory Trends are Often Lagging Indicators; Science and Consumer Trends are Leading Indicators

SEC disclosure principles focused principally on regulatory trends are not able to capture the most important trends regarding toxic chemicals, because science and private sector responses

¹² Apache and ACS GCI collaborate to advance greener fracking fluids, Richard Liroff, <https://www.greenbiz.com/article/apache-and-acsgci-collaborate-advance-greener-fracking-fluids>

are moving MUCH faster than US regulators. Although identifying trends in markets and even science are implicit in the MD&A, our observation is that regulatory trends are disclosed with far more rigor than science trends (hazard studies) or consumer preference shifts (i.e. the greening of consumer demand regarding a particular product).

The contrast between slow-moving regulation and fast-moving science is highlighted by the 2016 enactment of amendments to the Toxic Substances Control Act. The new law stipulates a framework for review of toxic chemicals on the market. There are 80,000 registered chemicals. Under the new law, the EPA is required to review a minimum of 20 chemicals at a time, with seven years to complete each review. The EPA process of reviewing a specific chemical preempts states from regulating or keeping the chemical from market for at least three years or until the EPA review is complete.

In contrast to this sluggish federal regulatory process, other trends continue to move much more quickly — emerging science, consumer information campaigns, European regulators, and pre-existing and potential state regulations.¹³

Purchasers as Market Drivers

Perhaps most significantly, some large companies are making decisions that are substantial drivers of markets and market trends. For example, Walmart and Target, two retailers with stores in every U.S. state, each have established business practices geared toward eliminating products with toxic ingredients. These firms have substantial market power — Walmart operates 6,200 stores and Target about 1,800.

Walmart announced in April that it has removed 95 percent of the 10 highest priority chemicals targeted by its pioneering Sustainable Chemistry Policy. This is striking progress, since Walmart announced its goal to eliminate these chemicals just two years ago.¹⁴ To our knowledge there has been little disclosure of these strong trends and pressures on the producers and sellers of affected products to Walmart and Target, nor of chemical companies whose demand is constricted by the big companies' decisions.

We believe these material effects on companies should be a clear-cut scenario for disclosure in MD&A because it may limit access to a major market. Yet, in our experience, few manufacturers or chemical producers are disclosing such consumer and science trends.

Emerging Science Trends Demand Disclosure

A substantial body of emerging scientific literature demonstrates the risk of certain nanotechnology materials. Where several peer-reviewed articles or credible government

¹³ <https://www.greenbiz.com/article/what-new-chemical-safety-law-means-business>

¹⁴ Walmart grows the chemical footprint movement
Richard Liroff, <https://www.greenbiz.com/article/walmart-grows-chemical-footprint-movement>

compilations of public health data demonstrate a potential catastrophic outcome from the use of a material, the accumulated information should suffice to trigger disclosure requirements, but the record is replete with 10-K reports that failed to disclose such trends. We have long recommended that additional guidelines be provided by the SEC on these points.¹⁵

As an example, the nanotechnology field is developing rapidly. Its applications include toothpaste, cosmetics, food processing, and food packaging. As a food additive, nanoparticles could deliver flavor, nutrition, medicines and supplements to existing food products. However, such materials also bring with them special health risks, which the scientific community is studying as these products emerge.

Nano-particles [particles smaller than 1,000 nanometers (nm)] are often more chemically reactive than their larger-scale counterparts. Specifically, as particle size decreases so dramatically, materials can penetrate the body far more aggressively. Laboratory studies indicate that some nanoparticles – be they inhaled or ingested from food and water – can pass through the intestinal walls or lungs and reach the bloodstream. Some inhaled nano-materials can access the brain, as they can pass the blood-brain barrier via the olfactory nerve.¹⁶

Specifically, nano-scale particles could infiltrate far finer biological shields than could ultrafine particles, enabling them to reach a greater surface area of human tissue than less fine substances.

One example of special concern is a material known as Carbon Nanotubes (CNTs). These materials are very useful in many technologies because they make materials that are light and strong. However these materials also top the list of potential mass tort catalysts because certain forms – specifically long, thin CNTs – possess the same physical characteristics as the most hazardous types of asbestos known as amphiboles. The physical similarities between CNTs and amphibole asbestos have led some researchers to suggest that long, thin CNTs may be capable of inducing mesothelioma. Although mesothelioma cases are very unusual in the general public, they are not uncommon in populations who are exposed to the amphibole forms of asbestos.¹⁷

While all of the effects of nanoparticles are impossible to predict, these known toxicity risks mean that liability potential is significant. Indeed, some experts recommend that nanotechnology's liability potential matches that of asbestos. The Expert Forecast on Emerging Chemical Risks, a body of 49 experts across Europe, places nanoparticles at the top of the list of substances from which workers need protection.¹⁸ The world's second largest reinsurer, Swiss Re, deems nanotechnology risk on a par with asbestos risk, noting the ease of tracing toxins

¹⁵ We previously described ongoing disclosure challenges, including those raised here, in our 2009 report: *Bridging the Credibility Gap: Eight Corporate Liability Accounting Loopholes that Regulators Must Close*. <http://iehn.org/documents/EightLoopholes.pdf>

¹⁶ G. Oberdörster, E. Oberdörster, and J. Oberdörster, Nanotoxicology: An Emerging Discipline From Studies of Ultrafine Particles. *Environmental Health Perspectives* 113, no. 7 (2005): 823-839.

¹⁷ <http://www.jdsupra.com/legalnews/nanotechnology-and-asbestos-informing-i-72106/>
“Nanotechnology and Asbestos: Informing Industry’s Approach to Carbon Nanotubes, Nanoscale Titanium Dioxide, and Nanosilver.” Catherine Morris, December 1, 2012

¹⁸ Nanotechnology is a major concern for European health experts, Nanowerk, March 27, 2009
<http://www.nanowerk.com/news/newsid=9846.php>

directly to a manufacturer – by contrast to more diffuse pollutants.¹⁹ Similarly, Lloyd’s of London deems the emerging risk of nanotechnology as grounds for close attention, risk evaluation, and disclosure.

In April 2013 the National Institute for Occupational Safety and Health, wrote:

In this Current Intelligence Bulletin, NIOSH continues its long-standing history of using the best available scientific information to assess potential hazards and risks and to provide guidance for protecting workers.... studies of animals exposed to CNT and CNF that are informative in predicting potential human health effects consistent with ways in which scientists traditionally have used such data in recommending risk management strategies. NIOSH systematically reviewed 54 laboratory animal studies, many of which indicated that CNT/CNF could cause adverse pulmonary effects including inflammation (44/54), granulomas (27/54), and pulmonary fibrosis (25/54) (Tables 3–1 through 3–8). NIOSH considers these animal study findings to be relevant to human health risks because similar lung effects have been observed in workers exposed to respirable particulates of other materials in dusty jobs [Rom and Markowitz 2006; Hubbs et al. 2011]. There are well established correlations between results of animal studies and adverse effects in workers exposed to particulates and other air contaminants [NIOSH 2002, 2006, 2011a, b]. Moreover, in animal studies where CNTs were compared with other known fibrogenic materials (e.g., silica, asbestos, ultrafine carbon black), the CNTs were of similar or greater potency [Lam et al. 2004; Muller et al. 2005; Shvedova et al. 2005; Murray et al. 2012], and the effects, including fibrosis, developed soon after exposure and persisted [Shvedova et al. 2005, 2008; Porter et al. 2010; Mercer et al. 2011]. These are significant findings that warrant protective action.²⁰

Recommendation: Include More Prescriptive Guidance for Disclosure of Emerging Science and Risks.

A hybrid of a principled and prescriptive disclosure rule or guidance, more prescriptive than the current MD&A, could substantially improve the quality of disclosure in this area:

1. Describe any trends in scientific studies (Peer-reviewed literature or government sponsored literature reviews or public health risk reports) that indicate potential for substantial health or environmental risks associated with the preparer’s products or activities. An example from nanotechnology manufacture and use would be for a user of carbon nanotubes to disclose evidence that some “carbon nanotubes” have been found to affect lungs through materials structurally similar to asbestos. Such disclosure should be made when three or more peer reviewed scientific studies indicate a serious health risk from a particular produced or widely used material, for instance.

¹⁹ George W. Pearson, “The Cost of Uncertainty: Nanotechnology Could be Risky Business,” RMI Newsletter (Volume 7, No 1) <http://www.asse.org/assets/1/7/GeorgePearsonArticle.pdf>

²⁰ National Institute for Occupational Safety and Health, CURRENT INTELLIGENCE BULLETIN 65 Occupational Exposure to Carbon Nanotubes and Nanofibers, April 2013.

2. Qualitatively and quantitatively describe the scope of potential exposure. While precise quantification of risk may be impossible for nascent technology, investors should know the extent of a company's potential exposure – e.g., how many people may be exposed and what portion of the company's activities involve use of the material in question.
3. Describe measures the company is taking to prevent, reduce, or mitigate the risks of potential long-term effects on reputation, demand, liability or regulation. Such measures could include seeking insurance, promoting exposure controls, funding research, testing or modifying the materials, etc. Investors should know, for instance, that Continental Western Insurance Group announced in 2008 that it would not cover nanotechnology-related risks, citing nanotube dangers specifically.²¹

III. Response to Concept Release Question 217

Would Line Item Information Be Immaterial?

217. Would line-item requirements for disclosure about sustainability or public policy issues cause registrants to disclose information that is not material to investors? Would these disclosures obscure information that is important to an understanding of a registrant's business and financial condition? Why or why not?

Recommendation: Even Though Financial Impact on Value Varies from Sector to Sector, Line Item Disclosures on Sustainability Are Appropriate and Remain Material

Judicial decisions and SEC practice make it clear that materiality is determined by whether the information in question would have been viewed by the reasonable investor as substantially altering the total mix of information made available, such that it could alter the reasonable investor's decisions – to buy or sell shares, for instance, or to vote a certain way on a proposal.

In today's investing marketplace, increasing attention is being paid to how to encourage companies to develop and disclose a clear long-term strategy for value creation. For instance, Blackrock CEO Larry Fink has sent a letter to chief executives at S&P 500 companies and large European corporations asking them to lay out for shareholders on an annual basis their strategic framework for long-term value creation. His letter specifically identified the role of ESG data as part of the assessment of long-term strategy.²²

As such, sustainability data are inherently material to investor interests, regardless of whether one is able to quantify the near-term impacts on financial performance. Efforts such as those by SASB to identify near-term financial materiality of disclosure topics are constructive, but they should not be mistaken for evidence that line item requirements on sustainability and public policy metrics would lead to immaterial disclosures.²³

²¹ http://www.vorys.com/media/publication/104_Nanotechnology%20Excluded%20from%20Insurance.pdf

²² <http://www.businessinsider.com/blackrock-ceo-larry-fink-letter-to-sp-500-ceos-2016-2>

²³ In our opinion, comments submitted by SASB on the Concept Release on July 1, 2016 reflect an inappropriately narrow perspective on materiality. SASB wrote in response to this question that: "Line-item requirements are generally not appropriate for sustainability issues because sustainability issues are likely not material for all

While SASB focused on financial materiality at the firm level, other disclosure frameworks which include definitions of materiality giving greater consideration to non-investor input, or less detailed analysis of financial impact, are still of material interest to the reasonable investor. In short, there is not reasonable justification for concluding that corporate social responsibility reports are either full of entirely immaterial information or irrelevant to investor scrutiny.²⁴

For large pension funds and other investors which are universal investors, broadly invested in the marketplace, the manner in which an individual investment may affect its entire portfolio, or may affect the economy as a whole, are “material” information which go beyond the question of how a specific fact may affect the value of the individual registrant. Similarly, for the ever-growing portion of investors that actively engage with their portfolio companies on matters of the environmental and social impact of the registrant’s operations, information on sustainability is of great concern and interest, regardless of whether it impacts a material portion of the individual registrant’s valuation.

Disclosures by a company related to externalities such as unregulated pollution, even if the externalities are not expected to be internalized any time soon, can certainly be material to buy and sell decisions by investors even though the externalities are not expected to effect the value of that company directly. This is especially the case with a set of considerations related to sustainability, which by definition encompass the economy/society-wide consequences of company actions. These issues are of concern because they present “portfolio risk” or systemic risk, regardless of whether they will affect the registrant’s valuation.

The Securities and Exchange Commission would be well served to create line items under Regulation S-K that go beyond information sought in the MD&A. The current MD&A rules focus solely on the impact of an issue on an individual company’s operations and finances. This is a narrower scope for disclosure of information than is relevant to reasonable investor understanding of the company’s management of major sustainability challenges such as environment, human rights and governance issues.²⁵

companies; when they are material, they manifest in unique ways and thus require industry-specific metrics.” In contrast to this comment, we believe appropriately drafted line item requirements in regulation S-K can leave flexibility for disclosure of relevant and material data for any company and that many line item requirements are materially important to investors regardless of the level of documented financial impact.

²⁴ While SASB’s focus on the impact of information on an individual company’s valuation can certainly yield useful information to companies and to investors, the scope of its standards are not congruent with materiality, but rather represent a narrower set of disclosures than of interest to the reasonable investor.

²⁵ Regulation S-K, which sets forth the specific disclosure requirements associated with Form 10-K and other SEC filings, requires that companies describe known trends, events, and uncertainties *that are reasonably likely to have material impacts on their financial condition or operating performance* in the Management’s Discussion and Analysis of Financial Condition and Results of Operations (MD&A) section of Form 10-K or 20F.

Sustainability disclosures reveal material information for the reasonable investor when they address information that may relate to the future value of the company in the short and long term, but also if they inform investors of the impact of the company on our world, including an investor's other holdings as well as the investor's reliance on a clean and sustainable economy.

Various sustainability metrics are relevant, crosscutting metrics material to investors even if they do not as dramatically affect value for some companies and sectors than in others. As noted above, a substantial portion of today's "reasonable investors" consider the societal impact of their investments, their portfolio wide impacts and long-term implications on the economy. Two examples of prescriptive line item disclosures that investors currently seek for all registrants and that IEHN would support include:

Political contributions disclosure (and lobbying) - SEC Petition 4-637-2
Scope 1, 2 and 3 Greenhouse Gas emissions

These are starting examples of data points that are material because a substantial portion of investors currently seek this data for all companies throughout the investing marketplace. The differential degree of impact on finances of different companies is irrelevant to whether or not such line items are material.

IV. SEC Concept Release Question 14 Identifying Audience for Materiality

14. Concept Release Question 14. Should we revise our rules to require disclosure that is formatted to provide information to various types of investors in a manner that will facilitate their use of disclosure for investment and voting decisions?

A. The audience targeted by a registrant's disclosures should be clarified by the registrant, including whether the firm considers socially responsible investors among those targeted in its determinations of materiality

In some areas of the Concept Release there is a sense that current rules, or potential rules regarding sustainability, would result in too much disclosure of "immaterial" information. We believe this is based on a distorted understanding of investor interest and audiences for reporting. For instance, if the definition of materiality is based on determination of whether a "reasonable investor" would want access to the information in the total mix of information, one next needs to consider what range of investors are "reasonable" investors. In light of the growing portion of the investment marketplace which makes investing decisions based on a company's impact on society as well as its impact on financial returns, the definition of materiality for purposes of a sustainability question seems to turn on whether the interest of an investor whose focus includes impact on society is among those "reasonable" investors to consider.²⁶

²⁶ In contrast, the SASB has taken an unfortunate turn in a different direction on this question, focusing solely on whether a sustainability issue would affect the company's bottom line. This is a mistaken interpretation of materiality, and should not be adopted by the Securities and Exchange Commission.

The Securities and Exchange Commission should address the lack of clarity and transparency regarding the decision-making factors that go into a firm's materiality assessments, including its interpretation of "reasonable investor"

The SEC and judicial interpretations are directed toward information that would influence the judgment of a "reasonable person" or a "reasonable investor." There is no single template for a "reasonable investor;" the determination of materiality is currently decided with opaque determinations to decide materiality – what investors, time horizons, types of risks considered or excluded based on uncertainty, magnitude of risk to the firm, etc. Failure to clarify these factors causes confusion in materiality assessment and contributes to the misperception that current disclosures include "excess" or "immaterial" disclosures.

Materiality determinations are based on numerous, generally unarticulated assumptions -- much more of an art than a science. Materiality is not an objective determination and there should be no pretense that it is. Disclosure must meet the needs of a very diverse array of users with different risk tolerances, time horizons, strategies, perspectives and concerns. And, the determination is made by a gatekeeper with a strong interest in non-disclosure. A Harvard Business School working paper, Materiality in Corporate Governance: The Statement of Significant Audiences and Materiality by Robert G. Eccles and Tim Youmans²⁷ suggests that registrants be required to file a "Statement of Significant Audiences and Materiality," ("The Statement") which would help in some instances to explain how materiality determinations are made. The authors noted:

When issuing "The Statement" the board must make judgments, tough judgments, since it cannot claim that all audiences are significant. Saying "We will create value for our shareholders by meeting the needs of all of our stakeholders" is not a Statement, it is puffery. It is greenwashing. A corporation, no matter how large, has limited resources and has to set priorities in terms of how they are allocated. For example, a corporation may choose to lay off employees or cut back on its R&D expenses in order to meet its quarterly earnings target. Implicitly, this is making short-term shareholders a more significant audience than employees or than long-term shareholders who would benefit from this research. Or the firm can have a different view, such as cutting dividends before "downsizing." Short-term shareholders may not like this decision, but long-term investors (e.g., pension funds) might applaud it. The Statement should also be clear about the time frames in which the corporation evaluates the impact of its decisions on its significant audiences. A 10-year horizon is very different than a one-year horizon.

The determination of materiality may be based, for instance, on a company's assumption that short term investors are driving the company's stock price, and therefore the only information that is deemed material is information relevant to quarterly returns, or more generously, a 3-5 year timeline. Alternatively, companies less concerned about meeting the quarterly earnings estimates of analysts and who are focused on delivering returns over a 3-5 year time frame are likely to consider a different set of information as material.

²⁷ http://www.hbs.edu/faculty/Publication%20Files/16-023_f29dce5d-cbac-4840-8d5f-32b21e6f644e.pdf

Determining materiality should consider the array of investors focused on the company and reading the report.²⁸ What are the array of investment scenarios and considerations that merit treatment as material? Does the firm consider investors that may hold shares in the company for the next 15 years? Does it consider investors that are using environmental, social and governance (ESG) matters as a proxy for management quality? Does it consider the investors who are making buy and sell decisions based on long-term considerations such as climate change, and therefore for instance, considering the extent to which a company is committed to growing its reserves of fossil fuels? Does it consider investors driven by ethical concerns, such as socially responsible, religious or mission-driven investors?

There is strong evidence in today's financial statements, and in the record of the recent financial crisis, to support the conclusion that in the absence of transparency of materiality determinations, determinations of materiality and disclosure are commonly manipulated by, among other things, delayed quantification, narrowed time horizons, and narrow interpretation of the "reasonable investor" to whom the data is of interest. The SEC is duty bound to rectify this problem.

Recommendation: Require a Statement of Significant Audiences and Materiality

We recommend that the SEC require transparency regarding the process registrants use to determine "material" disclosures. Each reporting company should include in its filing a description clarifying how it determines materiality:

- Groups or categories of investors to whom materiality assessments are directed,
- Relevant time frames,
- Rationales,
- Issues of known or potential interest to significant subgroups of investors.

In addition, recognizing that financial disclosures are also a key source of information to other constituencies, the SEC rules should allow reporting companies, in their discretion, to identify other audiences of investors or stakeholders to whom the disclosures have also been addressed.

Sincerely,

/S/

Sanford Lewis
General Counsel
IEHN

²⁸ Also, in its fiduciary duty of impartiality, a board may not be allowed to favor, for example, short-term investors over long-term investors, but obliged to consider the group of "all investors". Disclosure of materiality considerations would aid companies and boards in documenting how they apply this fiduciary duty.