ISSUE BRIEF

Sustainability Accounting Standards Board (SASB) Fall 2017

Accounting for Sustainability

It's hard to imagine a time when accounting practices were not closely monitored and regulated, yet this was the case until the mid-1900s. After the stock market crash in 1929, support began to build for the creation of uniformly accepted accounting standards. Many people speculated that distorted financial statements had led to mispriced stock prices, and ultimately the market downturn and succeeding Great Depression. This widespread accounting fraud and lack of investor confidence gave rise to the Securities Acts in '33 and '34, and eventually the Financial Accounting Standards Board (FASB).

Modern Day Accounting

Another revolution in accounting standards is building steam, and this time it relates to the disclosure of sustainability risks. In 2010, the Initiative for Responsible Investment at Harvard University conducted research on the financial materiality of sustainability information and developed industry indicators to measure these factors. As a response to this study, the Sustainability Accounting Standards Board (SASB) was founded in 2011 to serve as an independent organization that governs sustainability standards for 79 industries in eleven sectors. The mission of the SASB is to help public corporations disclose material, decision-useful information to investors in SEC filings[1]. The SASB is overseen by the SASB Foundation, whose notable Board of Directors includes Michael Bloomberg of Bloomberg LP, Mary Shapiro, Former SEC Chairman, Jack Ehnes, CEO of CalSTRS, and the former Chairman of the FASB, Robert Herz. The process of determining SASB's Standards has been evidence-based and market-informed. Both corporations and investors have weighed in on the process in an effort to create the most cost-effective and practical results.

On October 2, 2017, the SASB published the Exposure Draft Standards and opened up a 90-day public comment period. This feedback window allows the public to review and comment on the over 200 changes in order to help ensure the financial materiality and usefulness of the Standards for both corporations and investors. The SASB plans to finalize the methodology in the first quarter of 2018.

A Material World

One factor that has become ingrained in ESG investing is the concept of materiality. According to the U.S. Supreme Court, information is material "if there is a substantial likelihood that a reasonable shareholder would consider it important in deciding" when making investment decisions. Issues such as environmental sustainability or ethics used to be thought of as 'granola', and immaterial to financial performance. However, several decades of research have proven that ESG factors can indeed be linked to corporate profitability, and therefore deemed material.

The SASB has developed a Materiality Map™, which is an interactive tool designed to compare the importance of different sustainability issues across sectors and industries. An example of the Map at the sector level is shown on the previous page. This Map, along with the Standards, were developed using SASB's sustainability framework. The framework identifies five main categories of sustainability factors: Environment, Social Capital, Human Capital, Business Model and Innovation, and Leadership and Governance. A 2015 study conducted by Harvard Business School found that, using the SASB as a guideline, stocks that ranked highly on material sustainability issues outperformed stocks that had strong rankings on immaterial issues[2]. This finding, along with more recent research from Credit Suisse and Goldman Sachs, has helped make the case that considering sustainability issues when making investment decisions can be useful in the long run.

Sources:

[1]https://www.sasb.org/sasb/vision-mission/ *

[2]https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2575912*

DISCLOSURES