



# Standards Outcome Review

TRANSPORTATION

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SASB Standards Development Team  
March 18, 2014

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# Executive Summary

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This report provides a reference and framework for the SASB Standards Council Non Renewable Resources sector standards outcome review on March 25, 2014.

In the fourth quarter of 2013, SASB's Standards Development Team identified the material sustainability issues or disclosure topics) and related accounting metrics (herein after referred to as "issue(s)" and "metric(s)") that impact shareholder value in eight industries: Automobiles, Auto Parts, Car Rental & Leasing, Airlines, Air Freight & Logistics, Marine Transportation, Rail Transportation, and Road Transportation.

These issues and the associated accounting metrics have subsequently been vetted by external stakeholders through the Industry Working Group (IWG). This process allowed for each issue and metric to be evaluated on the basis of materiality, investor interest, and cost-benefit analysis. Based on this feedback and additional research, on April 17 SASB will open a 90-day public comment period (PCP) on accounting standards for the eight industries.

This report provides the Standards Council with an update on SASB's evaluation of IWG feedback and additional evidence research, which form the basis for a revised set of issues and metrics for public comment. **Table I** (next page) shows the list of issues by industry that were presented to the IWG and SASB's initial assessment and process for revising each of those issues

**Section I: Issues for Reconsideration** focuses on issues that received relatively low IWG feedback and where SASB will reconsider evidence of materiality based on IWG feedback and internal SASB research.

**Section II: Issues with Weaker Evidence of Materiality** provides SASB's review of, and response to, specific IWG feedback on issues for which there was general agreement about materiality, but where there were some reservations. **Section III** presents a summary of SASB's evidence research and decision whether to include additional issues proposed by IWG participants.

**Appendix I** contains a draft list of issues that SASB will present for public comment on April 17, 2014.

**Appendix II** provides sample accounting metrics for the Automobiles industry, for reference.

A supplement to this report provides a detailed materiality assessment of each disclosure topic by the IWG, and a list of all IWG comments on issues.

## Table I: Summary of IWG Feedback on Issues

	Automobiles	Auto Parts	Car Rental & Leasing	Airlines
# Issues	12	10	5	6
<b>Environment</b>	GHG Emissions & Energy Management	Energy Management		Air Emissions & Fuel Management
	Waste Management	Waste Management	Waste Management	
	Water Management	Water Management	Water Management	
<b>Social Capital</b>	Local Community Engagement			
			Passenger Safety	Passenger Safety
			Transparent Information & Fair Advice	Customer Experience & Transparent Information
<b>Human Capital</b>				Talent & Diversity
	Employee Health, Safety & Well-being	Employee Health, Safety & Well-being		
	Labor Relations	Labor Relations		Labor Relations
<b>Business Model &amp; Innovation</b>	Product Quality & Safety	Product Quality & Safety		
	Fuel Economy & Use-phase Emissions	Product Stewardship	Fleet Fuel Efficiency	
	Product End-of-life	Product End-of-life		
<b>Leadership &amp; Governance</b>	Competitive Behavior	Competitive Behavior		Competitive Behavior
	Supply Chain Management	Supply Chain Management		
	Fair Lending			
Emerging Issues				Regulatory Capture & Political Influence

SASB's initial assessment and process for reviewing each issue, following IWG:

*General agreement, with some reservations*

*Significant concerns, seeking additional evidence & inputs*

*Issue up for removal*

	Air Freight & Logistics	Marine Transportation	Rail Transportation	Road Transportation
# Issues	6	5	6	4
Environment	Air Emissions & Fuel Management	Air Emissions & Fuel Management	Air Emissions & Fuel Management	Air Emissions & Fuel Management
		Ecological Impacts	Ecological Impacts	
Social Capital			Community Relations	
Human Capital				Employee Recruitment & Retention
	Employee Health, Safety & Well-being	Employee Health, Safety & Well-being		Employee Health, Safety & Well-being
	Labor Relations		Labor Relations	
Business Model & Innovation				
Leadership & Governance	Business Ethics & Payments Transparency	Business Ethics & Competitive Behavior		
	Competitive Behavior		Competitive Behavior	
	Accident & Safety Management	Accident & Safety Management	Accident & Safety Management	Accident & Safety Management
Emerging Issues	Contractor Management	Climate Change Risk	Climate Change Risk	Climate Change Risk
		End-of-life		

SASB's initial assessment and process for reviewing each issue, following IWG:

*General agreement, with some reservations*

*Significant concerns, seeking additional evidence & inputs*

*Issue up for removal*

# I. Issues for Reconsideration

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This section focuses on issues that received relatively low IWG feedback (less than 75 percent of respondents agreed that the issue is material) and where SASB is reconsidering evidence of materiality based on IWG feedback and internal SASB research. Issues are analyzed by industry, looking first at **evidence of interest** from SASB’s heat map and detailed IWG feedback and second at **evidence of financial impact** from existing research in industry briefs complemented by additional research. An **assessment** of both types of evidence is then provided, together with a final **recommendation** for inclusion or removal of the issue.

## 1. AUTOMOBILES

### a. Issue: Water Management

#### *Evidence of Interest*

##### Heat Map tests

Score of 40 out of 100 for this issue, which is low relative to other issues in the industry.

##### IWG Feedback

- *Issue priority*

The average ranking of the issue was 9 out of 12, indicating that it was ranked lower than most issues in the industry.

- *Issue materiality*

Twenty out of 27 respondents (74%) agreed that it was a material issue. Five respondents said this issue was not material and two had reservations. Those who disagreed stated that it was 'already monitored and under control', that the automobiles is not as water intensive as other industries, and that there is not enough evidence of financial impact.

#### RESPONSES TO MATERIALITY OF WATER MANAGEMENT IN AUTOMOBILES INDUSTRY

	Corporation	Market Participant	Intermediary	Total	Percent of Total
<b>Yes</b>	3	9	8	20	74%
<b>No</b>	1	1	3	5	19%
<b>Maybe</b>	1	1	0	2	7%

#### *Evidence of Financial Impact*

##### Initial SASB Research (Excerpts of Industry Brief for IWGs)

As global production of vehicles grows, the demand for water continues to grow, even as the cost of accessing it increases. Automakers have employed various measures to reduce the burden on water resources, including harvesting rainwater, employing processes that use less water, and using recycled

water. For example, TATA Motors harvests rain water in order to reduce costs and maintain a reserve during times of water shortage. At the same time, only 13 percent of water used by the company is recycled or reused. At Subaru's Indiana plant, intelligent use of existing material saved 11 million gallons of water in 2006.

Auto OEMs are investing in technologies to reduce not only the water intensity of production but also the impact on quality of local water resources. Ford plans to reduce per vehicle water use to 4.0 cubic meters (or 1,056 gallons) by 2015, a 30 percent reduction from 2009 levels. In 2012, reduction in water use led to \$3 million in savings. At Ford's River Rouge factory near Detroit, water saving technologies costing \$15 million were installed. While the cost was high, it presented significant savings compared to the estimated \$50 million alternative of cleaning water runoff that was polluting a local river. At its \$500 million factory in Chennai, India, Ford used only 1.15 cubic meters of water for each vehicle produced in 2011. The plant operates a zero-discharge water recycling system, which separates the waste from water and disposes it as solid waste.

#### Additional Research:

- Cost of water as a fraction of operating costs
- Cost savings as a result of implementing processes to save, recycle, or reuse water
- Expenditures or disruptions in operations due to water shortage or scarcity
- Percent of operations in water-scarce regions to indicate forward-looking impact
- Water-intensity of industry compared to others
- Penalties, fines, or lawsuits against auto companies for discharging untreated waste into water ways
- Are there analyst reports or other sources that indicate that water-risk impact financial valuation?

#### **Findings**

- An analysis of Form 10-Ks of auto companies revealed a lack of disclosure on the topic.
- Over the lifecycle of a vehicle, the fraction of water used by auto manufacturers is small.
- Some Companies have operations in water-stressed regions and this issue could become more material if more production shifts to those regions. However, productions process are also becoming less water-intense (e.g. non-water based painting process) and therefore the industry may become less dependent on water.
- Water is not a key input to production and water intensity of production is declining.

**Recommendation:** Remove issue



## b. Issue: Local Community Engagement

### *Evidence of Interest*

#### Heat Map tests

Score of 25 out of 100, which is the lowest score for the industry and tied with supply chain management.

#### IWG Feedback

- Issue priority

The mean ranking of the issue is 12, indicating that the issue was ranked lower than all other issues.

- Issue materiality

IWG participants were roughly split between responding 'yes', 'no', and 'maybe' regarding materiality of the issue. Ten out of 27 respondents (37%) agreed to the materiality of the issue and 8 disagreed.

#### RESPONSES TO MATERIALITY OF LOCAL COMMUNITY ENGAGEMENT IN AUTOMOBILES INDUSTRY

	Corporation	Market Participant	Intermediary	Total	Percent of Total
<b>Yes</b>	2	4	4	10	37%
<b>No</b>	2	2	4	8	30%
<b>Maybe</b>	1	5	3	9	33%

- Comments from IWG respondents

#### SAMPLE COMMENTS FROM IWG PARTICIPANTS ON COMPETITIVE BEHAVIOR

Name	Response	Comment
██████████ Investor	Maybe	"Disputes with local communities are not common in the industry."
██████████ Corporation	No	"Local Community Engagement is definitely important to an automobile company, but even if a company does not reach out to the community in which it operates, the likelihood that it will have a material impact on the company is very low."
██████████ Intermediary	No	"Local community engagement is difficult to measure and currently practically impossible to compare, so the decision usefulness is very limited. Also, local community engagement in emerging countries is far more important than in developed countries, which makes the issue even more complex."
██████████ Intermediary	No	"There is not adequate evidence of this issue's financial impact on the industry that would justify further reporting requirements. The financial impact will be sufficiently shown in the financials, and the inclusion of text describing the potential long-term benefits/detriments will be of little use to investors. The traditional reasonable investor that is concerned with financial returns over social or environmental impact would not find such information material to an investing decision."

### *Evidence of Financial Impact*

#### Initial SASB Research (Excerpts of Industry Brief for IWGs)

Companies in the industry have used different methods to effectively engage with local communities in the regions where they have manufacturing operations. Some initiatives address both social and human capitals, while others address the management of supply chains, a wider governance issue. In its manufacturing plant in Tashkent, Uzbekistan, GM has established relationships with local high schools and universities in an effort to train the local population with skills needed to operate plant machinery. Similarly, Volkswagen works closely with local technical colleges in Tianjin, China, and trains teachers to “cover the medium-term demand for technically qualified experts in particular fields.” The company has also started collaborating with education centers near Puebla, Mexico, to train potential employees in advance to the opening of its Audi plant.

Efforts to engage with local stakeholders are not limited to current or future employees; automobile companies are also collaborating with local suppliers to increase the quality of auto components. This issue is particularly important for companies who are under a legal obligation to source a percentage of their components from local firms. Companies manufacturing vehicles in Russia, for example, are required to produce at least 30 percent of their vehicles with locally built engines. This issue is highlighted by Ford in its 2012 Form 10-K where they report that “many governments regulate local product content and/or impose import requirements as a means of creating jobs, protecting domestic producers, and influencing the balance of payments.” Close collaboration with suppliers is also relevant in the context of ensuring proper sustainability practices and performance along the value creating process; this aspect is addressed in the Supply Chain Management section in this brief.

In addition to local impacts due to the manufacturing operations, leading companies have also started to establish relationships with customers from emerging markets to understand local transportation needs. Ford talks about the need to engage with the new pool of customers in its 2012 corporate sustainability report: “The mobility needs of potential customers in emerging markets differ in some fundamental ways from those in the developed markets the auto industry has primarily served to date. Local community engagement is a key strategy Ford is using to learn about and understand how best to meet the needs of these critical and fast-growing markets.”

Finally, when an assembly plant closes, the impact on the local community is both broad and deep, including “decreased economic output, concentrated job losses and scars to the physical landscape.” Of the 447 automaker and automaker-captive<sup>1</sup> plants that have been in operation across the U.S. since 1979, only 180, or about 40 percent, remain in operation. According to a U.S. Department of Labor commissioned survey of 74 sites of repurposed auto manufacturing facilities, 72 percent of closed plants were among the top three employers in the community when they closed, a third employed more than 2,000 people at the announced time of closure, and over half employed between 400 and 999 people. The town of Flint in Michigan exemplifies the challenges when a major employer shrinks its operations. Flint went from having 80,000 GM workers at its peak in the 1970s to roughly 7,000 in 2008. In 2009, the city had a \$10 million budget deficit, 15.3 percent unemployment, and 1,400 acres of brownfields.

### **Assessment**

- Both weak evidence of financial impact (in brief), and weak evidence of interest.
- Additional research did not yield strong evidence of materiality and initial evidence was weak.
- No disclosure on this issue in Form 10-Ks.
- Any significant impacts on the community can be discussed in the management of environmental issues.

**Recommendation:** Remove issue

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<sup>1</sup> Auto maker-captive parts plants are plants owned by an automaker but operated as a separate division.

### c. Issue: Competitive Behavior

#### *Evidence of Interest*

##### Heat Map tests

This issue received a high score in the heat map test – 95 out of 100, behind only one issues (GHG emissions).

##### IWG Feedback

- *Issue priority*

The average ranking was 10 out of 12 issues.

- *Issue materiality*

Seventeen of the 27 respondents (63%) agreed that this is a material issue for the industry and seven respondents disagreed.

The issue was generally supported by market participants (8 out of 11 agreed on materiality of the issue) and public interest/intermediaries. However, only one (Honda) out of five corporations agreed that the issue was material.

#### RESPONSES TO MATERIALITY OF COMPETITIVE BEHAVIOR IN AUTOMOBILES INDUSTRY

	Corporation	Market Participant	Intermediary	Total	Percent of Total
<b>Yes</b>	1	8	8	17	63%
<b>No</b>	3	3	1	7	26%
<b>Maybe</b>	1	0	2	3	11%

Some IWG participants who did not agree on the materiality of competitive behavior felt that the issue needed to be better defined, while others did not see it as sustainability issue. A few responses from those who thought that the issue may be material (responded Yes or Maybe) are shown below.

- *Comments from IWG respondents:*

#### SAMPLE COMMENTS FROM IWG PARTICIPANTS ON COMPETITIVE BEHAVIOR

Name	Response	Comment
Market Participant	Yes	“Antitrust behaviors delays innovation by discouraging it, which itself is a long-term risks by distorting the real market value of the products. It also unfairly disadvantage consumers with excessive pricing and triggers a large-scale regulatory action with huge fines.”
Market Participant	Yes	“Investors need transparency on anti-competitive penalties and practices.”
Intermediary	Maybe	“The issue is not clear, as all businesses should thrive for competitive behaviour to succeed, i.e. to thrive to seek competitive benefits or advantages. The automotive industry does not seem to be influenced by more than average competitive behaviour, because the differences between the products are rather small. The differences between the OEMs are more a result of the management capabilities - VAG has clearly better management than GM, etc. It could be argued that the anti-competitive behaviour is a problem in the industry, because the standards and the OEM requirements make it difficult to enter the business.”

██████████ Corporation	Maybe	“While considerable laws exist that have impact on the industry, such as anti-trust laws and dealer franchise laws, in our opinion the competitive behavior issue is very steady-state and predictable.”
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## **Evidence of Financial Impact**

### Initial SASB Research (Excerpts of Industry Brief for IWGs)

There have been a number of investigations and fines assessed against car manufacturers for price-fixing, most notably outside the U.S. In 2011, Turkey’s competition board imposed a cumulative €108.5 million fine on 15 automobile companies and distributors for sharing information on sales targets and price strategies during a time of high demand for cars. Among these, Ford Otosan, a Ford and Koc Holding joint venture, was fined the highest amount of approximately €25 million. In 2013, the Korean Fair Trade Commission fined several manufacturers of large commercial vehicles for fixing prices between 2002 and 2011. As a result, Hyundai Motor was fined €48.3 million, Scania Korea €11.8 million, Volvo Group Korea €11.4 million, and Daimler Trucks Korea €3.2 million.

In the U.K., the Office of Fair Trading fined Daimler’s Mercedes-Benz unit and four of its commercial vehicle dealers £2.85 million for coordinating prices and exchanging commercially sensitive information between March 2007 and January 2010. In January 2012, Spain’s antitrust authority fined Suzuki €1.88 million for exchanging prices for certain motorbikes with Honda in 2009.

In the U.S., car dealerships enjoy exclusive rights to sell in an assigned area and so are not incentivized to sell at competitive prices. A study by the Federal Trade Commission concluded that dealership laws had a detrimental effect on customers by increasing prices by about six percent. The opposition faced by Tesla further highlights the anti-competitive nature of this relationship and the laws protecting dealerships. Until now, car dealerships have been successful in lobbying to limit competition. When local dealerships were threatened by potential competition from car sales over the Internet in the 90s, the industry successfully lobbied for state laws making it illegal for businesses to sell cars online in a market where it did not already have a local dealership.

Exclusive distributorship agreements, such as those between car manufacturers and dealerships, are not usually illegal under U.S. antitrust laws. However, these arrangements may violate antitrust laws if they substantially lessen interbrand competition or create monopoly in a line of commerce. The Department of Justice sued Dentsply International, an artificial tooth manufacturer, for violating antitrust laws and maintaining monopoly power in the market through its exclusive distributorship agreements with dealers. This case has set a precedent for sanctioning dominant firms in any industry that restrict access to a significant portion of a relevant market, efficient distribution channels, or scarce retail space.

### Additional Research:

- Are there domestic cases of anti-competitive behavior (price-fixing, etc) on any automobile company?
- Is there more evidence of domestic companies engaged in anti-competitive behavior domestically or abroad?

### **Assessment:**

- Evidence of financial impact is fairly strong, however IWG feedback is mixed, with low priority given to the issue.
- Research did not reveal additional cases of anti-competitive practices within the industry.
- While the barrier to entry is high for the market and only six automobile companies are listed in U.S. exchanges, there is sufficient competition in most markets.

**Recommendation:** Further research needed. Retain issue if industry characteristics make it prone for anti-trust practices since recent cases against auto manufacturers is not sufficient to chronic nature of the problem.

#### d. Issue: Fair Lending

##### *Evidence of Interest*

###### Heat Map tests

- N/A

###### IWG Feedback

- Issue priority

The mean ranking for Fair Lending was 11 out of 12 issues, placing it ahead of Local Community Engagement.

- Issue materiality

Just about half, or 14 out of 27 respondents agreed that the issue is material to automobiles industry. Eight respondents did not think the issue is material.

Nearly half of respondents in each stakeholder type agreed that the issue is material.

###### RESPONSES TO MATERIALITY OF FAIR LENDING IN AUTOMOBILES INDUSTRY

	Corporation	Market Participant	Intermediary	Total	Percent of Total
<b>Yes</b>	2	6	6	14	52%
<b>No</b>	2	4	2	8	30%
<b>Maybe</b>	1	1	3	5	19%

- Comments from IWG respondents:

###### SAMPLE COMMENTS FROM IWG PARTICIPANTS ON FAIR LENDING

Name	Response	Comment
██████████ Market Participant	Yes	“It’s particularly relevant for the US like, multi-racial societies with history of discrimination in terms of access to capital/finance. There is a clear litigation risks with large-scale damages while reputational risks are also very high.”
██████████ Market Participant	Maybe	“Haven’t come across this issue yet in automotive industry yet. Haven’t seen any evidence how this can negatively effect long term stock performance. [sic]”
██████████ Intermediary	Maybe	“Even if the scope of the standard is to serve a US investor, the US cases of fair lending problems should not be exaggerated, because the motor industry groups listed in the US have a large share of their sales outside the USA, and the fair lending is not such an issue in most parts of the world.”
██████████ Market Participant	No	“Post-2008 relaxed lending practices can be under scrutiny, and regulations in this space should hold industry participants sufficiently accountable, but if only certain considerations should be chosen as most important, this should not be one of them”

##### *Evidence of Financial Impact*

###### Initial SASB Research (Excerpts of Industry Brief for IWGs)

In order to prevent discriminatory lending practices and to ensure transparency, the financing arms of auto companies will continue to face scrutiny from the Consumer Financial Protection Bureau. According to the Bureau, the fact that the improper decisions may be made by auto dealers—who are exempt from consumer bureau oversight—does not absolve lenders of responsibility for resulting racial disparities.

The Bureau and the DOJ are examining lending operations of major auto manufacturers. According to the National Consumer Law Center (NCLC), a series of national class action lawsuits brought under the Equal Credit Opportunity Act resulted in settlements valued at well over \$100 million. The NCLC cites cases settled by Daimler Chrysler Financial, Toyota Motor Credit Corporation (TMCC), Ford Motor Credit Company, General Motors Acceptance Corporation, Nissan Motors Acceptance Corporation, and American Honda Finance Corporation (AHFC). In 2006, TMCC, AHFC, and WFS Financial, Inc. settled a nationwide class action lawsuit regarding discriminatory lending practices against African-American and Hispanic consumers. The settlement included, among other provisions, cash or credit payments of up to \$400 per class member, broad refinancing to reduce rates charged to current customers whose markups are one percent or greater, and donations of \$1.9 million to non-profit organizations involved in consumer education and assistance.

The financing arm of motor companies is vital for auto makers to maintain sales. As GM states in its 2012 Form 10-K, “We intend to rely on GM Financial to support additional consumer leasing of our vehicles and additional sales of our vehicles to consumers requiring sub-prime vehicle financing.” The filing also highlight the tension between using financing arms to drive sales and maintaining fair lending practices, stating that “GM Financial faces a number of business, economic, and financial risks that could impair its access to capital and negatively affect its business and operations and its ability to provide leasing and sub-prime financing options to consumers to support additional sales of our vehicles.”

#### Additional Research

- Identify portion of sales/revenue from U.S. and abroad, either for a few top companies or on an industry-level
- Compared to the revenues of these companies, the penalties (from the current evidence) do not seem material. Find more evidence of penalties and fines related to discriminatory lending to illustrate chronic nature of this issue.
- Find examples of corporations actively managing this issue (e.g. by limiting the discretionary markup).

#### **Findings**

- IWG feedback is mixed, with low priority given to the issue.
- Strength of evidence of financial impact, heat map tests, and additional research.
- Additional evidence research confirms the evidence discussion in the brief. There are additional instances of class action lawsuits and companies settling discriminatory lending cases out of court.
- An analysis of 10-K filings indicate that companies are proactive about managing this issue and being in compliance with Truth in Lending Act, the Equal Credit Opportunity Act and the Fair Credit Reporting Act.

**Recommendation:** Retain issue

## 2. AUTO PARTS

### a. Issue: Competitive Behavior

#### ***Evidence of Interest***

##### Heat Map tests

The issue received a score of 60 out of 100, which was the second highest score for an issue in this industry.

##### IWG Feedback

- *Issue priority*

The issue was ranked lowest among the 10 issues for this industry.

- *Issue materiality*

Seven of the 11 IWG respondents (64%) agreed that the issue was material and only one participant disagreed.

While there is more support for this issue from market participants and public interest/intermediaries, corporations were split on this issue. Two agreed that it is a material issue, two disagreed, and one said that they had reservations.

#### RESPONSES TO MATERIALITY OF COMPETITIVE BEHAVIOR IN AUTO PARTS INDUSTRY

	<b>Corporation</b>	<b>Market Participant</b>	<b>Intermediary</b>	<b>Total</b>	<b>Percent of Total</b>
<b>Yes</b>	2	2	3	7	64%
<b>No</b>	1	0	0	1	9%
<b>Maybe</b>	2	1	0	3	27%

All but one survey respondent thought that the issue is or may be material, and overall respondents gave low priority to the issue. Kimberly Bowden of Delphi Automotive who disagreed with the materiality of the issue commented, "In my opinion competitive behavior is what determines a companies [sic] economic viability and is key to the operational survival of a company."

#### ***Evidence of Financial Impact***

##### Initial SASB Research (Excerpts of Industry Brief for IWGs)

There are several recent high-profile cases of market manipulation by auto parts companies. According to its 2012 annual report, Autoliv entered into a plea agreement with the U.S. Department of Justice (DOJ) and paid \$14.5 million in fines for two counts of violations of antitrust laws involving a Japanese subsidiary. As a result, the company is also being investigated by representatives of the European antitrust authority, the Competition Bureau of Canada and the Korean Fair Trade Commission for antitrust behavior among suppliers of occupant safety systems. Similarly, in 2012, TRW Automotive Holdings agreed to plead guilty to one count of conspiracy in restraint of trade involving sales of occupant safety products and to pay \$5.1 million to settle antitrust violations with the DOJ.

In October 2012, Japanese auto parts maker Tokai Rika Co. agreed to plead guilty and pay \$17.7 million in fines for its involvement in price-fixing. Another large auto parts supplier, Denso, also agreed to plead



guilty to the DOJ's ongoing investigation into price-fixing and bid-rigging. Denso has agreed to pay a criminal fine of \$78 million for violations of antitrust laws in connection with sales of certain automotive components. Another Japanese supplier, Yazaki, will pay \$470 million for violation of the Sherman Act. In addition, four Yazaki executives will serve prison time for their involvement in the violations. In November 2001, Furukawa Electric pleaded guilty and was fined \$200 million for its role in price-fixing and bid-rigging.

The sheer number of investigations and confirmed cases of violations of antitrust laws by auto parts suppliers indicate the chronic nature of this problem. In February 2010, E.U. antitrust regulators investigated Lear Corporation, Leoni AG, and their competitors for suspected price-fixing. Several suppliers and auto executives have been found guilty in similar investigations. In July 2013, Ford sued Fujikara for setting artificially high prices on wire harnesses supplied to them from 2000 to 2010.

According to a DOJ press release, "(t)o date, nine companies and 14 executives have pleaded guilty or agreed to plead guilty in the department's ongoing investigation into price-fixing and bid-rigging in the automotive parts industry." The companies were sentenced to pay a total of more than \$809 million in criminal fines and 12 individuals have been sentenced to pay criminal fines and to serve jail sentences ranging from a year and a day to two years each. According to the plea agreements, the companies have agreed to assist the DOJ with the current investigations. The European Commission and authorities in other jurisdictions are also looking into antitrust violations related to the DOJ investigations.

#### Additional Research

- Clarification from industry experts: SASB will follow up to gain further understanding of feedback from Kimberly Bowden.

#### **Findings**

- Evidence of financial impact is strong, however there was not overall agreement on the issue.
- Additional evidence research confirms the evidence discussion in the brief.
- Top companies in the industry reported investigations and lawsuits regarding alleged anti-competitive behavior in the EU (Visteon Corporation FY2011), Canada (Visteon Corp. FY2012), and India (China Zenix Auto International FY2012)
- Recent regulatory action and ongoing investigation into anti-competitive behavior by auto parts companies make the issue material for the industry.

**Recommendation:** Retain issue.

### 3. CAR RENTAL & LEASING

#### Overview

Car Rental & Leasing is a unique industry with two global players listed in U.S. exchanges, Avis and Hertz. Much of the evidence is therefore limited findings about these companies and Enterprise, a privately-held corporation. While both Avis and Hertz participated in the industry working group, there were only five survey respondents in total, including three public interest or intermediary stakeholders. There was no participation from investors or other market participants. Of the five issues presented to the IWG, only two passed the 75 percent threshold with four out of five participants agreeing on each issue. These are the tangible issues of water and waste management. The rest, Passenger Safety, Transparent Information & Fair Advice, and Fleet Fuel Efficiency, are discussed below.

#### a. Issue: Passenger Safety

##### *Evidence of Interest*

##### Heat map tests

Passenger Safety received a relatively low score of 25 out of 100 in the heat map tests.

##### IWG Feedback

##### - Issue priority

Survey respondents ranked the issue 2<sup>nd</sup> in priority after fleet fuel efficiency. There were five issues for this industry.

##### - Issue Materiality

Two of the five respondents agreed that the issue is material to the industry, while two disagreed.

Both the corporations disagreed that the issue is material to their industry, citing that the issue is material to OEMs and the excellent safety record of the industry.

##### RESPONSES TO MATERIALITY OF PASSENGER SAFETY IN CAR RENTAL & LEASING INDUSTRY

	Corporation	Market Participant	Intermediary	Total	Percent of Total
<b>Yes</b>	0	0	2	2	40%
<b>No</b>	2	0	0	2	40%
<b>Maybe</b>	0	0	1	1	20%

##### - Comments from IWG respondents:

##### SAMPLE COMMENTS FROM IWG PARTICIPANTS ON PASSENGER SAFETY

Name	Response	Comment
██████████ Corporation	No	“Inclusion of passenger safety is outside of car rental ESG/sustainability key areas of interest and materiality. Safety equipment is material to OEMs and compliance with safety regulations fall under current 10-K reporting. Recommend removal of this section.”
██████████ Corporation	No	“The vehicle rental companies that account for the vast majority of this industry’s revenue all buy vehicles new, so their fleets are populated by vehicles that must adhere to the most recent safety regulations and standards. With very rare exceptions, the safety record of the car rental industry with respect to safety recalls is outstanding. In the meantime, proposed legislation is therefore aimed at the safest, best maintained

		cars, and does not contemplate all other fleet operators, including government fleets, commercial delivery fleets, private sector company cars, school buses, all of those vehicles are not subject to legislation and so this matter is material to those fleet operators for that reason.” [sic]
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**Evidence of Financial Impact**

Initial SASB Research (Excerpts of Industry Brief for IWGs)

Hertz mentions in their annual report that, “depending on the severity of any recall, it could materially adversely affect our revenues, create customer service problems, reduce residual value of the recalled cars and harm our general reputation.” Avis Budget highlights purchasing safer cars as a focus area in their annual report, stating, “we face risks associated with sourcing vehicles for our fleet and potential safety recalls affecting vehicles in our fleet.”

Avis Budget reports statistics in their Annual Report on the number of their technicians who are Automotive Service Excellence certified as 68 percent. Avis Budget states, “we place a strong emphasis on vehicle maintenance for customer safety and customer satisfaction reasons, and because quick and proper repairs are critical to fleet utilization.”

Car rental companies face competing incentives to reduce costs while also providing a high level of safety to customers. Enterprise was caught removing safety features from its car orders in order to save costs. The company offered rental cars to customers that were missing side airbags that are a standard feature in the model of the car. Enterprise had ordered the cars as part of a special order and removed the side airbags to save \$145 per vehicle. This type of action can upset customers who may be familiar with a particular car model and will have safety expectations based on standard features.

A group of U.S. Senators are working on a bill that would address rental car safety for the first time. The bill is currently awaiting review by both the House of Representatives and Senate. The Raechel and Jacqueline Houck Safe Rental Car Act of 2013 is named after two sisters that were killed in 2004 while driving a rental car that had been recalled for a power steering hose defect but had not yet been repaired. If passed, the new legislation will require that any, “rental vehicle subject to a safety recall cannot be rented or sold until the safety defect is remedied.” This type of legislative activity highlights the importance of safety best practices as a mechanism for staying ahead of legislation while also ensuring customer satisfaction.

In 1988, Hertz agreed to pay \$2.5 million in an out-of-court settlement to a man left paralyzed after a multi-car pileup caused by a stalled Hertz rental car. The stalled car had faulty wiring as the result of an earlier accident, and the wiring was never properly repaired. The then-renter of the car had visited two Hertz locations for a repair before the accident but was turned away after the car was deemed to be working properly.

To be conducted

**Assessment**

- Evidence of financial impact is fairly strong. IWG feedback is mixed, with high priority given to the issue.

**Recommendation.** Due to the unique nature of the industry and the composition of the industry working group, in depth discussions with corporations and market participants will inform the issue.

## b. Issue: Transparent Information & Fair Advice

### *Evidence of Interest*

#### Heat map tests

The issue received a relatively low score of 25 out of 100 on the heat map tests.

#### IWG Feedback

- *Issue priority*

Survey respondents ranked Transparent Information & Fair Advice 5<sup>th</sup> out of five issues for the industry.

- *Issue materiality*

One of the five respondents agreed that the issue is material to the industry, while two disagreed.

Both the corporations disagreed that the issue is material to their industry. One cited that the issue is outside the realm of sustainability while the other did not agree with the conclusions in the brief about the complexity of rental pricing.

#### RESPONSES TO MATERIALITY OF TRANSPARENT INFORMATION & FAIR ADVICE IN CAR RENTAL & LEASING INDUSTRY

	Corporation	Market Participant	Intermediary	Total	Percent of Total
<b>Yes</b>	0	0	1	1	20%
<b>No</b>	2	0	0	2	40%
<b>Maybe</b>	0	0	2	2	40%

- *Comments from IWG respondents:*

#### SAMPLE COMMENTS FROM IWG PARTICIPANTS ON TRANSPARENT INFORMATION & FAIR ADVICE

Name	Response	Comment
██████████ Corporation	No	“Outside of car rental sustainability KPIs - SASB guidance should be limited to ESG metrics.”
██████████ Corporation	No	“We disagree with the conclusions in your industry brief about this section. New consumers who may not have rented or leased a vehicle can be confused by the way pricing is presented, but the vast majority of consumers understand that base prices are no more the entire price than restaurant menu items represent the final total for a meal. Every purchase involves taxes and fees and consumers understand that. The way the rental car industry presents prices has been reviewed and approved by a number of attorneys general and is an industry standard procedure in place for many years that does not create significant customer service problems. Again, this is an area that is important to us as a company and to our customers, but it is not a material issue for a reasonable investor.”

### *Evidence of Financial Impact*

#### Initial SASB Research (Excerpts of Industry Brief for IWGs)

Hertz agreed to pay just over \$11 million in a July 2013 settlement of a class action lawsuit regarding transparency of their fees for their PlatePass electronic toll payment service. The suit alleged that Hertz failed to inform their customers that they were required to pay a service fee for each day they rented a car

containing a PlatePass, even if they did not use the system. One customer claimed that she was billed \$77.75 for the system and was not informed of the cost when she rented the car. While Hertz denies all claims, they agreed to pay \$11,004,000 settlement and over \$3 million in legal fees for the Plaintiffs.

Avis has given the issue attention in their 2012 Form 10-K, stating, “we launched Avis Preferred Select & Go™, a vehicle-choice program for customers, revised our rental agreements and receipts to improve transparency, and significantly expanded customer-service-oriented training of our employees, and we achieved significant increases in customer satisfaction. We expect to continue to invest in these efforts in 2013. The company also reports that the use of the Internet by cost-conscious customers has, and will continue to, increasingly allow them to obtain and compare rates more easily, especially as regulations around transparency evolve. “This transparency,” the company says, “may increase the prevalence and intensity of price competition in the future.”

#### *Additional Research*

To be conducted

#### ***Assessment***

- Evidence of financial impact is weak and not sufficient to illustrate substantial impact of the issue on the financial performance of auto rental companies.

#### ***Recommendation***

Due to the unique nature of the industry and the composition of the industry working group, in depth discussions with corporations and market participants will inform the issue.

**c. Issue: Fleet Fuel Efficiency**

***Evidence of Interest***

Heat map tests

The issue received 38 out of 100 in the heat map test, which is the highest for the issues in this industry.

IWG Feedback

- Issue priority

The issue was ranked in first place, indicating highest priority.

- Issue materiality

Three of five respondents agreed the issue is material, while two did not.

**RESPONSES TO MATERIALITY OF FLEET FUEL EFFICIENCY IN CAR RENTAL & LEASING INDUSTRY**

	Corporation	Market Participant	Intermediary	Total	Percent of Total
<b>Yes</b>	1	0	2	3	60%
<b>No</b>	1	0	1	2	40%
<b>Maybe</b>	0	0	0	0	-

- Comments from IWG respondents:

**SAMPLE COMMENTS FROM IWG PARTICIPANTS ON FLEET FUEL EFFICIENCY**

Name	Response	Comment
██████████ Corporation	Yes	“Note that most large rental companies have hundreds of thousands of cars. If ZEV, PZEV data is not currently being tracked, it could require extensive internal resources to report on this data. Also, revised standards for GHG and Smog ratings have only been required at the Federal level for 2013 models and newer. It could be a few years before rental fleets are fully converted to 2013 models and newer, especially for value brands which typically hold many older vehicle models. Also note that although high fuel economy vehicles are desirable to many customers, the consumer demand for alternative fuel vehicles, other than hybrids, is lagging. Additionally, AFVs have higher purchase prices and often rental companies cannot apply for rebates; and do not enjoy the fuel cost savings these vehicles provide - this savings is passed directly onto the customer, while the higher operating cost lies with the rental company.”
██████████ Corporation	No	“This is possibly the biggest error in your brief. The fuel efficiency of a particular vehicle is of interest to SOME customers, as discussed below; the fuel efficiency of our FLEET is irrelevant to customers; and investors care about whether our fleet is diversified enough and sized to meet customer demand with good utilization. Fleet fuel efficiency, we know from years of experience as a public company, is not a significant investor concern. With respect to consumers, based on our experience, the customers who care significantly about fuel efficiency are a relatively small minority who are looking to do anything and everything they can to minimize the cost of travel. Environmental issues have limited impact on customers' decision making, according to our research. That's why the number of gas/electric hybrids in our fleet has gone DOWN over the past few years, the lack of demand. Ditto electric vehicles, which are also not in demand. It's important to note

		that there are very different dynamics at work when people are renting a car for a business or leisure trip compared with securing a vehicle for their home day-to-day use. People who have saved all year for a vacation may splurge on a fancy vehicle to enhance their time off while opting for a plug-in hybrid for their driveway to minimize their emissions. Business travelers also frequently have different needs (more luggage, different weather conditions, multiple adult passengers) when they are traveling compared to their day-to-day needs in their home lives.”
██████████ Intermediary	No	“Fleet fuel efficiency is a great advertising motto for the company. The problem is that if a company is not using fuel efficient cars, the impact to the company is not as great as if there was some damage to other people or the environment. This should not be considered material until 2016 if a company is not complying with the laws that require more fuel efficiency mandated to be 54.5 mpg by 2025.”

**Evidence of Financial Impact**

Initial SASB Research (Excerpts of Industry Brief for IWGs)

Rental car companies are facing growing demand from customers for fuel efficiency. A national survey published in April 2013 by the Consumer Federation for America indicates that consumers strongly support higher mileage standards, and expect high fuel economy in their next car purchase. Car rental companies that do not stay on pace or ahead of consumer purchasing preferences may find themselves viewed as offering antiquated products and may lose market share.

Most major rental car companies offer fuel efficient rental options, including electric vehicles and hybrids. The Hertz Dream Car rental program recently started offering the Tesla Model S at a rate of \$400 per day. Avis requires that 100 percent of their economy, compact, and intermediate car classes meet the U.S. EPA’s SmartWay Certified requirements. The company also offers different models of gas/electric hybrid vehicles and flex fuel cars for those customers that wish to reduce their environmental footprint through the use of ethanol fuel.

Interestingly, the Form 10-Ks of the two U.S. domiciled publicly traded companies, Avis and Hertz, include the same exact disclosure regarding fleet fuel efficiency. “The U.S. Congress and other legislative and regulatory authorities in the United States and internationally have considered, and will likely continue to consider, numerous measures related to climate change and greenhouse gas emissions. Should rules establishing limitations on greenhouse gas emission or rules imposing fees on entities deemed to be responsible for greenhouse gas emissions become effective, demand for our services could be affected.” Hertz goes slightly further on this issue to say, “our fleet and/or other costs could increase, and our business could be adversely affected.”

Additional Research

To be conducted

**Assessment**

- Evidence of financial impact is weak. IWG feedback is mixed, with high priority given to the issue.

**Recommendation**

Due to the unique nature of the industry and the composition of the industry working group, in depth discussions with corporations and market participants will inform the issue.

## 4. AIRLINES

### a. Issue: Talent & Diversity

#### *Evidence of Interest*

##### Heat map tests

Talent & Diversity received 55 out of 100 in the heat map test, placing it ahead of only the customer experience and transparent information issue.

##### IWG Feedback

###### - *Issue priority*

The mean ranking of the issue by IWG respondents is low, at 6<sup>th</sup> place among the six issues for the airlines industry.

###### - *Issue materiality*

Thirteen out of 22 respondents (59%) agreed that the issue was material and three respondents disagreed.

Out of the five corporate respondents, three thought it was material issue and two had reservations about it materiality (response: 'Maybe, but I have substantial reservations').

#### RESPONSES TO MATERIALITY OF TALENT & DIVERSITY IN AIRLINES INDUSTRY

	<b>Corporation</b>	<b>Market Participant</b>	<b>Intermediary</b>	<b>Total</b>	<b>Percent of Total</b>
<b>Yes</b>	3	6	4	13	59%
<b>No</b>	0	0	3	3	14%
<b>Maybe</b>	2	2	2	6	27%

###### - *Comments from IWG respondents:*



SAMPLE COMMENTS FROM IWG PARTICIPANTS ON TALENT & DIVERSITY IN AIRLINES INDUSTRY

Name	Response	Comment
██████████ Corporation	Maybe	"I think Talent should be bundled with Labor Relations as a workforce issue. Yes, pilot and other potential labor shortages are material, as your issue brief suggests. However, I do not believe the evidence is there to support "diversity" being a material factor to investors at this time. Thus, I think Diversity should be dropped and "Talent" or "Workforce" should be grouped with Labor Relations."
██████████ Market Participant	Maybe	"The evidence would seem to support the importance of maintaining and growing an airline company's pool of "talented" pilots as the demand for these will likely be growing. However, I don't think that other classifications of employees present this level of materiality and likely do not need disclosure on how the issues of talent and diversity are being considered and managed."
██████████ Intermediary	No	"I feel that Talent and Diversity is an important issue, there are limitations. As stated in the article, the talent pool is not as diverse as it could be meaning that the staff will not be diverse. This kind of hiring and retaining practices can be voluntary, but not required."
██████████ Intermediary	Yes	"Labor relations and Talent & Diversity are closely linked (via supply and demand). The trend will be to spend more on preparing for demographic, political, and social pressures. For an industry that operates on such small margins, there will be material positive impacts on those airlines that are proactive and effectively address coming human capital shortages – and negative impacts on those who don't."

**Evidence of Financial Impact**

Initial SASB Research (Excerpts of Industry Brief for IWGs)

Airlines are facing two important trends that threaten their pilot talent pool: increasing federal requirements for minimum pilot training and reductions in working hours to diminish fatigue and higher-than-normal retirement rates driven by an aging population of pilots. Additionally, female pilots constitute a small portion of the entire pilot population.

New federal regulations have significantly increased the number of flight hours required to hire pilots, and in 2014, they will begin requiring more daily rest time. These regulations mean airlines will have to hire 5 percent more pilots. Estimates for the number of pilots needed to fill this gap vary from 60,000 to 65,000 in the next eight to ten years.

Statements in AMR Corp's FY2012 10-K highlighted the effect of pilot shortages on airlines, stating the risks of limited talent supply by saying that "in the past, we had to reduce capacity and take other steps in an effort to reduce the impact of pilot retirements. If pilot retirements were to exceed normal levels in the future, it may adversely affect us." Given the ICAO's Next Generation of Aviation Professional's announcement on high retirement levels, this issue is likely to have an increasing effect on airlines through 2026.

Given the higher-than-normal retirement rates, airlines are losing their most experienced employees. In response, airlines are paying close attention to talent and include diversity as a performance metric for top executives. Delta Airlines 2012 Form 10-K lists "supporting diversity" as a performance review criteria for Vice Presidents and Senior Vice Presidents.

Additional Research

The diversity angle needs to be explored further in order to establish this as a sustainability issue.

- Some IWG members suggested that the talent component of the issue was material but not the diversity angle.
- Talent & Diversity is a sustainability issue due to the diversity issue. Without diversity, the issue becomes a purely business issue. In that case, the pilot shortage evidence could be folded into the labor relations issue. (see comment below by Nancy Young)
- Need to prove the case for diversity in the industry
  - Is there a wage gap between male and female pilot with same years of experience?
  - What is the retention rate for female pilots (compared to male pilots)?
  - Are there any success stories of airlines turning around the shortage by recruiting female pilots actively?
  - Are there any studies that show that a gender-balanced (or otherwise diverse) cockpit crew is better in crisis situations?
  - Conversely, are there any instances where male-dominated crew made a bad decision that could've been prevented if a more balanced crew was present?

**Assessment**

- While the issue of pilot shortage is material, it appears to be a business issue. Research did not reveal any systemic discrimination against minorities or women.

**Recommendation**

Delete this issue in light of the recommendations by IWG respondents and further research.

**b. Issue: Competitive Behavior**

***Evidence of Interest***

Heat Map tests

Competitive Behavior scored the highest among Airlines industry issues. It received 80 out of 100 in the heat map test.

IWG Feedback

- *Issue priority*

It received a mean ranking of five out of six issues, just ahead of Talent & Diversity.

- *Issue materiality*

Sixteen of the 22 respondents (73%) agreed that competitive behavior is a material issue for the industry. Four respondents disagreed.

While there is support for this issue from market participants and public interest/intermediaries, corporations were split on this issue. Two agreed that it is a material issue, two disagreed, and one said that they had reservations.

RESPONSES TO MATERIALITY OF COMPETITIVE BEHAVIOR IN AIRLINES INDUSTRY

	Corporation	Market Participant	Intermediary	Total	Percent of Total
<b>Yes</b>	2	7	7	16	73%
<b>No</b>	2	1	1	4	18%
<b>Maybe</b>	1	0	1	2	9%

- *Comments from IWG respondents:*

SAMPLE COMMENTS FROM IWG PARTICIPANTS ON COMPETITIVE BEHAVIOR

Name	Response	Comment
██████████ Corporation	No	“Traffic data from the Department of Transportation ( <a href="http://www.transtats.bts.gov/DL_SelectFields.asp?Table_ID=264&amp;DB_Short_Name=Air Carrier Summary">http://www.transtats.bts.gov/DL_SelectFields.asp?Table_ID=264&amp;DB_Short_Name=Air Carrier Summary</a> ) shows that between 2002 and 2012, the largest carriers (AA, UA, DL, WN, US) have shown flat growth while several new airlines, including Frontier, Spirit and Allegiant have more than doubled in size. Other medium sized airlines, such as Alaska and Hawaiian have had double digit increases. This data does not indicate an industry that is uncompetitive or has significant barriers to entry. In addition, finding only 1 examples of a US antitrust suit that has not been settled, and which the airline may eventually win, does not indicate that this is a pervasive problem (the example of the Emirates suit is not relevant to US carriers since US carriers cannot sell tickets between Australia and the UAE). The discussion of slots in the Competitive Behavior section of the Brief is not material to this issue. There are only a handful of slot constrained airports in the US. Certain airports establish slots due to capacity constraints and due to pressure from local communities to avoid noise. Airport authorities control how many slots are allocated, not airlines. New airlines can have access to slots by purchasing them from incumbent airlines.”
██████████ Corporation	No	“Mergers and Alliances are a fact. They are very mature -- meaning that this industry knows how to do these things. The instances where there may be a violation of antitrust rules are very rare. In any event, if they

		<p>rise to materiality as a financial matter, they already are reported under existing rules and protocols. The "evidence" of the U.S. DOJ case regarding the US Airways-American merger is not compelling. That case was providentially brought, without relevant support and was settled under terms that the industry expected. See. e.g., <a href="http://www.forbes.com/sites/airchive/2013/11/14/the-winners-and-losers-of-the-us-airways-american-merger/">http://www.forbes.com/sites/airchive/2013/11/14/the-winners-and-losers-of-the-us-airways-american-merger/</a>"</p>
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## **Evidence of Financial Impact**

### Initial SASB Research (Excerpts of Industry Brief for IWGs)

In the context of recent consolidation and reorganizations through bankruptcy, certain airline industry practices have been scrutinized by anti-trust authorities, including market concentration, predatory pricing, and the anti-competitive effects resulting from airline alliances and mergers.

U.S. Airways is currently in the spotlight with federal regulators over its pending merger with American Airlines. The Justice Department filed a suit in Washington federal court seeking to permanently block the merger. Federal courts are examining whether the merger would lead to less competition in the industry and higher prices for consumers. U.S. Airways currently holds 55 percent of the slots at Reagan National Airport; post-merger that would increase to 69 percent. However, U.S. Airways and AMR Corp argue that there are two other major airports serving the Washington metropolitan area, and post-merger, they would only control 25 percent of aircraft seats into the market. The news of the government's antitrust suit caused U.S. Airways stock to fall 13 percent, and bonds of American's parent company AMR Corp. also dropped. AMR Corp, which filed for bankruptcy in November 2011, is using the merger as a means to complete a reorganization and exit court protection.

The issue is also affecting other companies in the industry. In its 10-K filing for 2012, Southwest Airlines states that "AirTran is currently subject to pending antitrust litigation, and if judgment were to be rendered against AirTran in the litigation, such judgment would adversely affect the Company's operating results." The litigation is a 2009 class action suit that accused AirTran of colluding with Delta airlines in 2008 to fix baggage fees.

Regulatory scrutiny of anti-competitive practices extends beyond the U.S. and affects airlines' global operations. A federal court in Australia fined Emirates, the UAE based airline, \$10.2 million in 2012 for price-fixing. The court found that the airline, based in the United Arab Emirates, had engaged in cartel conduct with other carriers by fixing prices associated with fuel and other surcharges in its routes to Australia. This example exposes that U.S.-based airlines are engaged in a global business and can be held accountable for their actions in any country in which they operate. The penalty comes from the Australian Competition & Consumer Commission (ACCC), who imposed a total of \$68 million in fines to Emirates and the other airlines involved in the cartel.

### Additional Research

- Based on the response from corporations, sector lead will reach out to respondents to clarify this issue.
- Based on the comments below, evidence section should be strengthened.
- In particular, it would be good to find more evidence of penalties due to anti-competitive behavior in the US
- Find cases where new airlines found it difficult to enter the market due to the existing mono/duo/oligopoly
- Studies to show that market concentration has led to loss of consumer surplus, higher (non-competitive) prices for consumers.

**Assessment**

- IWG feedback is mixed, with low priority given to the issue.
- Additional research supports feedback from IWG respondents.
- While the industry is characterized by high barrier to entry, airlines merging and airline alliances, proposed mergers have generally been allowed on terms of the consent decree.
- Mergers are generally well-publicized and pertinent information regarding proposed and allowed mergers is available to investors.

**Recommendation**

Delete issue.

## 5. AIR FREIGHT & LOGISTICS

### a. Issue: Competitive Behavior

#### *Evidence of Interest*

##### Heat map tests

Competitive behavior received a score of 40 out of 100 in the heat map tests. Only the issue of air emissions and fuel management received a higher score among issues in the industry.

##### IWG Feedback

###### - *Issue priority*

The mean ranking of the issue tied it with Employee Health, Safety and Well-being in fourth place out of six issues.

###### - *Issue materiality*

Nineteen out of 27 respondents (70%) agreed that this is a material issue for the Air Freight and Logistics industry. Five respondents did not agree that this is a material issue.

Most respondents within each stakeholder group agreed that it is a material issue.

#### RESPONSES TO MATERIALITY OF COMPETITIVE BEHAVIOR IN AIR FREIGHT & LOGISTICS INDUSTRY

	Corporation	Market Participant	Intermediary	Total	Percent of Total
<b>Yes</b>	5	7	7	19	70%
<b>No</b>	1	3	1	5	19%
<b>Maybe</b>	2	0	1	3	11%

###### - *Comments from IWG respondents:*

#### SAMPLE COMMENTS FROM IWG PARTICIPANTS ON COMPETITIVE BEHAVIOR

Name	Response	Comment
██████████ Market Participant	No	“For UPS and FedEx, the competitive environment is relatively well understood by investors. The investment community is already aware of the possibility for collusive practice between airfreight and ground players. The 3PL space is generally competitive and fragmented enough to create pricing competition, despite the DoJ fine in 2010. This is particularly true in freight brokerage, where the top 10 players control only 43% of the ~\$45 billion US market.”
██████████ Corporation	Yes	“Competative behavior is critcal in this space - international trade restrictions can cripple this idustry and so can unfair trade practices - governments in several parts of the world support parcel delivery fixed costs with mail revenues and even though they are in some cases billions of dollars in the red they continue to compete with unfair advantages in waht is suppose to be a "free market", some use political favortism to promote an uneven playing field in a very competative markets. The EU restricted a major deal in Europe last year that goes against free trade and open competative market principals in logistics. Competition, Free trade and open markets have always proven to produce the best service and the best price for consumers - logistics is no different” [sic]

## ***Evidence of Financial Impact***

### ***Initial SASB Research (Excerpts of Industry Brief for IWGs)***

In recent years, many multinational freight forwarders faced hefty fines for cartel behavior and price-fixing. In 2010, the U.S. Department of Justice charged six international air freight and logistics companies with criminal price-fixing charges. The companies agreed to pay a combined total of \$50.27 million in criminal fines. The price-fixing fines came under the Sherman Act, which carries a maximum fine of \$100 million per offense for corporations. Following the swathe of fines from the U.S. government, the EU issued penalties to 14 companies for a total of 169 million Euros.

U.S.-based UTI Worldwide was one of the companies fined by the EU regulators. The company discusses anti-competitive behavior in their Form 10-K filing for 2012. The filings describe a history of investigations from various governments looking into alleged anti-competitive behavior and specifically note that the U.S. Department of Justice and the South African Competition Commission have recently closed their investigations on UTI with “no adverse findings. Investigations remain open in Brazil and Singapore and we have appealed a prior adverse decision of competition authorities in the EU.” The filings go further to describe financial impacts from a European Commission (EC) investigation of alleged anti-competitive behavior related to air freight forwarding services. UTI was notified on March 28, 2012, by the European Commission that the commission was imposing a fine of 3.1 million euro (approximately \$4.1 million at the time) on UTI and two of their subsidiaries. UTI has appealed the decision and fine.

Similarly, UPS and FedEx have also been challenged in courts for violations to U.S. antitrust law by allegedly conspiring to refuse to negotiate with third-party negotiators retained by shippers and by individually imposing policies that prevent shippers from using such negotiators.

### ***Additional Research***

- What are the levels of concentration for (1) air freight, (2) post and courier, and (3) transportation logistics segments of the industry? See comment on comp. behavior from Daniel Schuster, IWG respondent.
- Are there examples of penalties or anti-trust behavior on the part of (1) air freight or (2) transportation logistics companies?
- If the issue only applies to some segments of the industry, need to clarify that in the issue description.

### ***Assessment***

- Evidence of financial impact is fairly strong. IWG feedback is mixed, with low priority given to the issue.
- Additional evidence research confirms the evidence discussion in the brief.
- There are anti-trust cases involving cargo segment of commercial airlines.

### ***Recommendation***

Retain issue.

## 6. MARINE TRANSPORTATION

### a. Issue: Air Emissions & Fuel Management

#### *Evidence of Interest*

##### Heat map tests

N/A

##### IWG Feedback

- *Issue priority*

The issue was ranked 1, indicating highest priority, out of the five issues for the industry.

- *Issue materiality*

Eight of the 12 respondents (67%) agreed that the issue is material to the marine industry. Two respondents, including one corporation and one public interest participant, disagreed that the issue is material to the industry.

At a total of 12, the number of respondents was low for this industry. While most agreed with the materiality of the issue, the percentage in agreement did not cross 75 percent.

#### RESPONSES TO MATERIALITY OF FAIR LENDING IN AUTOMOBILES INDUSTRY

	Corporation	Market Participant	Intermediary	Total	Percent of Total
<b>Yes</b>	3	4	1	8	67%
<b>No</b>	1	0	1	2	17%
<b>Maybe</b>	0	1	1	2	17%

- *Comments from IWG respondents:*

#### SAMPLE COMMENTS FROM IWG PARTICIPANTS ON COMPETITIVE BEHAVIOR

Name	Response	Comment
██████████ Intermediary	No	“these issues are regulated by international bodies and companies would not exist if they were not in compliance, therefore these issues are satisfied prior to investment decisions.”
██████████ Market Participant	Maybe	“I think fuel management is material. I'm not sure air quality is one of the most material issues facing marine transport. According to the literature you provided, Marine Transport only accounts for 3% of global GHGs. My feeling is that this industry won't be targeted in terms of GHG emissions. Spills, groundings, species introduction seem to be far more of a worry.”
██████████ Corporation	Yes	“The high cost of fuel, compliant with US State regulations as well, is a material issue. This includes the high costs of investing in fuel alternatives, such as cold ironing. <a href="http://www.americanshipper.com/Main/News/Port_of_Long_Beach_ready_for_cold_ironing_rule_55554.aspx">http://www.americanshipper.com/Main/News/Port_of_Long_Beach_ready_for_cold_ironing_rule_55554.aspx</a> , and <a href="http://www.broward.org/Port/MasterPlan/Documents/PTI%20Cold%20Ironing%20Economics.pdf">http://www.broward.org/Port/MasterPlan/Documents/PTI%20Cold%20Ironing%20Economics.pdf</a> ” [sic]



## ***Evidence of Financial Impact***

### ***Initial SASB Research (Excerpts of Industry Brief for IWGs)***

Current U.S. regulations surrounding greenhouse gas emissions and fuel standards are driving an increase in capital investment in the marine shipping industry. Regulation is focused on limiting the sulfur content in fuel because of public concerns about air quality and smog, rather than broader GHG emissions reductions that are more difficult to target. This implies that shipping companies will have to purchase cleaner fuel. Investment is concentrated on new or upgraded diesel engines for existing and new vessels. The EPA estimates that the annual costs of its emissions-reduction programs for ships operating in U.S. waters was \$1.85 billion in 2010, rising to \$3.11 billion by 2030. Furthermore, the agency expects the cost of shipping a container trans-Pacific to rise by roughly \$18 due to regulations, or approximately 3 percent of current operating costs. These additional costs are expected to be passed on to consumers through higher freight rates. While the exact financial impacts cannot yet be determined, it is evident that the EPA regulation is of material concern to ship owners. Current disclosure on existing and emerging regulations on the topic in SEC filings is prevalent among the top companies in the industry, but not standardized.

Globally, estimated costs to the industry due to environmental regulation are considerable: the Chairman of the International Chamber of Shipping, Masamichi Morooka, stated in June, 2013 that the IMO's low-sulfur emissions requirements could cost the global shipping industry up to \$550 billion between 2015 and 2025. These costs would cover capital upgrades to comply with 0.5 and 0.1 percent sulfur content fuel requirements. The lower sulfur content reduces the amount of particulate matter and sulfur oxides emitted during combustion.

### ***Evidence Gaps***

- Relevant quotes from 10-K analysis
- Relevant regulations

### ***Assessment***

- IWG feedback is mixed, with high priority given to the issue but agreement on the issue was not overwhelming.
- Further research to be conducted; evidence of financial impact needs to be strengthened and issue angles clarified.

### ***Recommendation***

Retain issue, and address concerns raised by IWG respondents.

## 7. RAIL TRANSPORTATION

### a. Issue: Community Relations

#### *Evidence of Interest*

##### Heat map tests

Community Relations received a low heat map score of 20 out of 100, putting it behind the other rail industry issues.

##### IWG Feedback

- *Issue priority*

IWG participants ranked the issue 5<sup>th</sup> among six issues.

- *Issue materiality*

Just about half or twelve of the 22 respondents agreed the issue is material to the industry. Seven disagreed about the materiality of the issue.

Two corporations participated in the IWG. One of them agreed that it is a material issue since “Communities are becoming more vocal and knowledgeable and can have an influence on how a project proceeds.” The other considered it material issue only under special circumstances like a train derailment.

The rest of the input from corporations were in the form of a letter from the Association of American Railroads. On the issue of community relations, the letter stated “This is a very important issue that gets substantial attention and effort from railroads.” However, there was concern about an effective way of disclosing efforts to manage community relations to investors.

#### RESPONSES TO MATERIALITY OF COMMUNITY RELATIONS IN RAIL TRANSPORTATION INDUSTRY

	<b>Corporation</b>	<b>Market Participant</b>	<b>Intermediary</b>	<b>Total</b>	<b>Percent of Total</b>
<b>Yes</b>	1	6	5	12	55%
<b>No</b>	0	7	0	7	32%
<b>Maybe</b>	1	1	1	3	14%

- *Comments from IWG respondents:*

SAMPLE COMMENTS FROM IWG PARTICIPANTS ON COMPETITIVE BEHAVIOR

Name	Response	Comment
██████████ Intermediary	Yes	"Most urban centers experience rail operations. New rail infrastructure also is mostly associated with urban centers. Most urban centers have deaths at railcrossing. Derailments have been an issue."
██████████ Market Participant	Yes	"Grade crossing and potential hazmat accidents are clearly material. Grade separation projects can also be very expensive (i.e. material) from a capex perspective. Traffic congestion caused by long and frequent trains is also an issue that must be managed with communities."
██████████ Market Participant	Yes	"Can affect network fluidity and capex. For example, if communities along the EJ&E were somehow to effectively lobby to demand CN invest an extraordinary amount in noise reduction or grade crossing elimination, a project benefiting the broader rail industry and even the nation's transportation fluidity could have been NPV negative for CN, the investor."
██████████ Market Participant	Yes	"Given that rails go through people's backyards, the rails' social license to operate is very important, and events like Lac Megantic and the 2009 spill in Cherry Valley,IL ( <a href="http://www.schumer.senate.gov/Newsroom/record_print.cfm?id=345520">http://www.schumer.senate.gov/Newsroom/record_print.cfm?id=345520</a> ) lower the level of trust between the rail industry and communities."
██████████ Market Participant	No	"Community relations encompasses a number of issues and opportunities which, by themselves or in the aggregate, are not material to most investors. The metrics that potentially could be rolled into this category are also likely to be redundant with those of others, and I fear that skeptics would consider some of the metrics to be "squishy" and difficult to quantify and verify (i.e., outreach efforts, etc.)"

**Evidence of Financial Impact**

*Initial SASB Research (Excerpts of Industry Brief for IWGs)*

The US railroad network consists of over 140,000 miles of track. Annually, there is an average of 270 deaths at public and private crossings. While safety measures implemented by the FRA and railroad companies have reduced the number of fatalities by 54 percent over the last two decades, in an average year, 431 people die along railroad tracks. Trespassing along railroad rights-of-way is the leading cause of rail-related deaths in America, compromising approximately 95 percent of total rail-related fatalities.

Safety measures include the common-sense partnership between the US Department of Transportation and major railroads that aims to reduce the number of injuries and fatalities on tracks, and other public safety efforts to clear-cut vegetation along tracks to improve visibility. A handful of companies have started including disclosures regarding this issue in their SEC filings, including Union Pacific, Norfolk Southern and CSX. In particular, Norfolk provides investors with information on community awareness and emergency response programs it has implemented to minimize risks both to its license to operate and to local communities.

Community engagement can help avoid disruptions in operations and major project delays. In 2012, BNSF faced considerable community opposition to its planned Port of Long Beach rail yard. The rail yard is to be built in close proximity to two schools, a park, and residential neighborhoods. Residents were concerned with elevated levels of air pollution stemming from the estimated 5,500 trucks and numerous trains serving the yard. An environmental analysis conducted on the proposed project supported claims there would be significant impacts to air quality and noise. In May, 2013, the Los Angeles City Council approved the \$500 million project. Shortly thereafter, several entities, including the Long Beach City

Council and the National Resource Defense Council, filed suit against the city of Los Angeles on behalf of community groups, citing improper health impact assessments and violations of the California Environmental Quality Act. Although the suit is pending, the consequences from community opposition are likely to be significant, ranging from delays and additional cost to a potential ban on the project.

#### Additional Research

- Importance of community relations for rail project development.
- Evidence of erosion of rail companies' social license to operate.

#### **Assessment**

- IWG feedback is mixed, with low priority given to the issue.
- Additional research to be conducted.

#### **Recommendation**

Retention of the issue to be determined after additional research, including but not limited to, additional evidence work and discussions with industry experts.

## **b. Issue: Ecological Impacts**

### ***Evidence of Interest***

#### Heat map tests

Ecological Impacts received a heat map score of 25 out of 100, where it was tied with Competitive Behavior and ahead of Community Relations.

#### IWG Feedback

- *Issue priority*

IWG respondents ranked the issue low at 6<sup>th</sup> place out of six issues.

- *Issue priority*

Twelve out of 22 respondents (55%) agreed that ecological impact is a material issue for the industry. Seven respondents did not think ecological impact is a material issue for the industry.

Neither of the two corporations, Canadian National Railway and transport infrastructure developer Padeco, deemed the issue to be material for the industry. The other stakeholder groups were divided in their opinion.

#### RESPONSES TO MATERIALITY OF ECOLOGICAL IMPACTS IN RAIL TRANSPORTATION INDUSTRY

	<b>Corporation</b>	<b>Market Participant</b>	<b>Intermediary</b>	<b>Total</b>	<b>Percent of Total</b>
<b>Yes</b>	0	8	4	12	55%
<b>No</b>	1	6	0	7	32%
<b>Maybe</b>	1	0	2	3	14%

Among those who agreed that Ecological Impact is material, respondents commented that these are concerns during development of new railways and at railway terminals and fueling stations. Some felt that the issue was material from the perspective of accidents, an angle which is covered under Accident & Safety Management.

Those who disagreed, failed to see any impact on financial performance of companies. One commented that the fines were not large. One market participant commented, "While the individual risks associated with an ecological issue (i.e., derailment and spill) can be quite high, collectively I see little evidence that the aggregate effect in this area would be fully material to the average, reasonable investor. Further, the probability of such an issue occurring in an ecologically sensitive area are low."

### ***Evidence of Financial Impact***

#### Initial SASB Research (Excerpts of Industry Brief for IWGs)

Coal dust blowing off of rail cars may impact waterways and land along railroad tracks, despite preventative methods such as covering cars and spraying adhesive agents onto the coal. Burlington Northern Santa Fe Railroad estimates that between 60,000 and 120,000 pounds of coal is lost from a standard 120-car train travelling between Wyoming and Seattle. The Sierra Club brought a suit against BNSF in 2013 alleging violations of the CWA, because the company does not have National Pollutant Discharge Elimination Systems (NPDES) permits; the case is pending.

Similarly, in 2012, the EPA and Union Pacific Railroad settled a violation of the CWA for \$1.5 million. The EPA found the company had spilled coal and engine oil, as well as inadequately prevented storm-water

pollution at several of its rail yards. Given the extent of the US railroad network, the cumulative effect of coal and minor fuel spills represents a significant ecological impact.

#### Additional Research

- Do most companies develop/build and maintain their own railways?
- Is there any additional evidence regarding the environmental impact of fueling stations and terminals, like this evidence from the brief: “Similarly, in 2012, the EPA and Union Pacific Railroad settled a violation of the CWA for \$1.5 million. The EPA found the company had spilled coal and engine oil, as well as inadequately prevented storm-water pollution at several of its rail yards.”?
- Is there any evidence to support the view that these fines are chronic and not one-off, since the amount was not very high?
- Is there evidence of interest (from shareholders, etc) in this issue?
- Initially, during issue discussion we thought that there may be habitat fragmentation issues.
  - For example, do railways cut across natural migrations paths or habitat of an animal?
  - Are there statistics regarding animals killed by railway tracks?

#### **Assessment**

- Evidence of financial impact is weak. IWG feedback indicated low levels of consensus about the materiality of the issue and low priority.
- Additional research to be conducted

#### **Recommendation**

Retention of the issue to be determined after additional research, including but not limited to, additional evidence work and discussions with industry experts.

## II. Issues with Weaker Evidence of Materiality

For the issues below, around 75 percent of IWG members agreed about materiality. IWG comments were reviewed to see whether additional evidence-gathering was needed. The following provides recommendations on these issues based on the analysis of IWG feedback.

### 1. AUTO PARTS

#### a. Issue: Energy Management

Eight of the 11 respondents (73%) agreed that Energy Management is a material issue. The only respondent who disagreed is a public interest/intermediary. The survey respondent commented that, “Energy management is important; however, to the consumer or investor it is reflected in product costs.”

##### RESPONSES TO MATERIALITY OF ENERGY MANAGEMENT IN AUTO PARTS INDUSTRY

	Corporation	Market Participant	Intermediary	Total	Percent of Total
<b>Yes</b>	4	2	2	8	73%
<b>No</b>	0	0	1	1	9%
<b>Maybe</b>	1	1	0	2	18%

The issue was on average ranked second highest, after product quality and safety by IWG respondents.

In the Heat Map test, the issue received a score of 63 out of 100 – the highest score among all 10 issues in the industry.

**SASB will retain the issue given the strength of the evidence of financial impact in the briefs and evidence of interest.** The comment by the IWG respondent who disagreed with the materiality of the issue is in line with SASB’s analysis. As the value impact section states, “Cost of energy used in manufacturing of final products is included in the cost of goods sold (COGS). Environmental regulations may require auto parts manufacturers to increase capital expenditures (CapEx) in the short to medium term in order improve efficiency of their facilities and equipment. This would likely have a long-term benefit through significant savings on energy costs and substantially improve gross margins and operating results.”

#### b. Issue: Water Management

Eight of the 11 respondents (73%) agreed that Water Management is a material issue and none of the disagreed. Among those who agreed, one respondent stated that, “(w)ater, in certain areas of the world and globally, is becoming an area of risk for industry and for humanity. Although water is generally cheap, the risk factor makes it a material issue for investors.” The World Council on Sustainable Business Development also finds several risks to business due to water constraints including financial, operational, market, reputational and regulatory risks.

##### RESPONSES TO MATERIALITY OF WATER MANAGEMENT IN AUTO PARTS INDUSTRY

	Corporation	Market Participant	Intermediary	Total	Percent of Total
<b>Yes</b>	4	1	3	8	73%
<b>No</b>	0	0	0	0	-
<b>Maybe</b>	1	2	0	3	27%

The issue was ranked 9 out of 10 issues by IWG respondents.

Water Management received 30 out of 100 in the heat map test, where it is tied with Labor Relations and scores higher than Supply Chain Management.

**SASB will reconsider this issue and conduct further research in light of excluding it from automobiles industry.**



## 2. AIRLINES

### a. Issue: Customer Experience & Transparent Information

Seventeen out of 22 respondents (77%) agreed that Customer Experience and Transparent Information is a material issue for the airlines industry. However, four respondents (none of whom are corporations) did not agree. Among those who disagreed, commented:

- “Customer Experience and Transparency are viewed on a very temporal basis. Any material impact would be derived more from perceptions rather than well defined standards. In addition, the emerging regulations seem to have relatively minor financial impacts and enforcement appears more reactive than systematic. [sic]”
- “Customer Experience is not a material issue as it is more of a subjective outcome. Either customers know what their airline provides and accept it as their business model or else their expectations are not met in which case either the airline is lowering its standards or the passengers expectations are too low/high. It stands to reason that that transparent information allows passengers to make the best choices possible which of course is a consideration for customer satisfaction but does not necessarily have to be viewed as material to the airline. [sic]”

Another respondent shared a good lead for additional evidence and suggested splitting the issue:

“I would place these two issues separated since "Transparent information" is of high relevance for investors, while improving customer experience can be considered of highest relevance for business travellers. Due to their high frequency of flights and sometimes tight schedule, they are usually much more demanding in terms of added-value offered by airlines, which includes special care throughout the whole flying experience. Considering that business travellers are of high importance for every airline due to high prices they pay for flight tickets (sometimes five times higher than the price of a flight ticket in economy class), the lack of attention given to this issue may significantly affect the financial performance of airlines and consequently, the perception of investors. A recent survey conducted by Deloitte LLP ("Rising above the Clouds: Charting a course for renewed airline consumer loyalty") revealed that 72 percent of high-frequency business travelers participate in multiple programs, and over one-third participate in four or more programs. There continues to be a lack of customer centricity, relevancy and engagement in the airline industry; as their programs and focus on the experiences are lacking for the individuals. See more at: <http://loyalty360.org/resources/article/the-challenge-to-create-loyalty-and-relevancy-in-the-airline-industry#sthash.5cWXEbFp.dpuf> [sic]”

#### RESPONSES TO MATERIALITY OF CUSTOMER EXPERIENCE & TRANSPARENT INFORMATION IN AIRLINES INDUSTRY

	Corporation	Market Participant	Intermediary	Total	Percent of Total
<b>Yes</b>	4	7	6	17	77%
<b>No</b>	0	1	3	4	18%
<b>Maybe</b>	1	0	0	1	5%

Out of the six issues, IWG respondents ranked it third behind Air Quality & Fuel Management and Passenger Safety.

Customer Experience & Transparent Information received a relatively low score of 44 out of 100 in the heat map test, placing it at the bottom of the six issues for the industry.

**SASB will reconsider inclusion of the issue. Evidence of financial impact is weak and the sustainability angle of the issue needs to be articulated better.**

### 3. AIR FREIGHT & LOGISTICS

#### a. Issue: Business Ethics & Payments Transparency

Twenty-one out of 27 respondents (78%) agreed that the issue is material to the industry. Only two respondents, both market participants, disagreed.

#### RESPONSES TO MATERIALITY OF BUSINESS ETHICS & PAYMENTS TRANSPARENCY IN AIR FREIGHT & LOGISTICS INDUSTRY

	Corporation	Market Participant	Intermediary	Total	Percent of Total
<b>Yes</b>	6	8	7	21	78%
<b>No</b>	0	2	0	2	7%
<b>Maybe</b>	2	0	2	4	15%

The issue ranked high among IWG respondents, it was in second place after Air Emissions & Fuel Management.

The heat map score for Business Ethics & Payments Transparency was 40 out of 100.

- Establish link between Sarbane's Oxley and this issue as mentioned by an IWG respondent, "Sarbane's Oxley must be used as the indicator of this issue rather than duplicate existing methods which produce the results to indicate this practice exist. Enforcement of the SOX penalties makes more sense than adding another layer."
- Find evidence on payments transparency from AGMs. See IWG comment, "Logistics provider operate globally, including sensitive countries with high corruption risks. Given time sensitivity of shipments, incentives to act contrary to business ethics standards i.e. to clear customs faster to avoid (further) delays etc. is higher relative to other industries. Transparency over payments (incl. lobbying activities) came up at AGMs last year, i.e. for UPS which indicates increasing shareholder concern."

**SASB will retain the issue, but will add to evidence based on IWG respondent feedback.**

## 4. RAIL TRANSPORTATION

### a. Issue: Competitive Behavior

Seventeen of the 22 respondents (77%) agreed that the issue is material for the rail industry. The rest five disagreed that it is a material issue. Both the corporations agreed that it is a material issue for the industry.

#### RESPONSES TO MATERIALITY OF COMPETITIVE BEHAVIOR IN RAIL TRANSPORTATION INDUSTRY

	Corporation	Market Participant	Intermediary	Total	Percent of Total
<b>Yes</b>	2	11	4	17	77%
<b>No</b>	0	3	2	5	23%
<b>Maybe</b>	0	0	0	0	-

There was good feedback on the issue from IWG respondents.

#### COMMENTS FROM IWG PARTICIPANTS ON COMPETITIVE BEHAVIOR

Name	Response	Comment
██████████ ██████████	Yes	Competitive Behavior has two aspects. The first is the usual competition versus competing transportation providers, usually trucking companies but also other railroads and barge in some instances. The other is regulatory. Railroads have some degree of exemption from anti-trust statutes that enables them to exclude other railroads from commercial use their tracks. Shippers frequently challenge this in front of the STB and recently Congress (Senator Rockefeller) has put forth legislation to force freight railroads to allow other railroads to provide commercial service on their lines, often referred to as "open access."
██████████	No	Competitive behavior is only an issues when rails are seen as charging too much for services for shippers with little competitive choices.

Competitive Behavior was ranked 4<sup>th</sup> out of six issues for the industry.

It received a heat map score of 25 out of 100, placing it ahead of Community Relations with a score of 25.

**SASB will likely retain the issue, clarify the issue angle, strengthen the evidence section and highlight the specific channels of impact.**

## 5. ROAD TRANSPORTATION

### a. Issue: Employee Recruitment & Retention

Nineteen out of 24 respondents (79%) agreed that the issue is material to the industry. Two respondents disagreed.

The issue was ranked 4<sup>th</sup> out of four issues for the industry.

Employee Recruitment & Retention received a heat map score of 35 out of 100.

While many respondents agreed that it was a material issue due to high turnover rates (of around 100%), one of two respondents who disagreed commented, “We don’t think that Employee Recruitment & Retention is a material issue from an investor perspective, unless the reporting company has a particularly poor performance record in this area. And if that’s the case, the reporting would likely have to disclose any significant business-related risks due to recruitment/retention in their 10-K filings anyway.”

**SASB will retain the Employee Recruitment & Retention issue because of strong evidence of interest (only two respondents out of 24 disagreeing about materiality) and evidence of financial impact.**

### b. Issue: Employee Health, Safety & Well-being

Eighteen out of 24 respondents (75%) agreed that the issue is material to the industry. Four respondents disagreed.

The issue was ranked 3<sup>rd</sup> out of four issues for the industry.

Its heat map score of 40 out of 100 put it ahead of Employee Recruitment & Retention.

Those who disagreed did not find the financial impact on companies to be significant.

**SASB will retain the Employee Health, Safety & Well-being issue because of relatively strong evidence of interest and will conduct additional research to strengthen the evidence of financial impact. Based on feedback from Delta Series workshop participant, SASB will research the added angle of disease migration via truck drivers.**

# III. Additional Issues Proposed by IWG Participants

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The following additional material issues were suggested by industry working group members, and reviewed by SASB. This is followed by SASB's decision on the issues, based on additional evidence research.

1. Automobiles
  - a. VOC Emissions – new angle to air emissions issue
2. Airlines
  - a. Community Relations
3. Air Freight & Logistics
  - a. Political Contributions
4. Rail Transportation
  - a. Trafficking – drugs and other contraband
  - b. Supply Chain Management
  - c. Waste Management – rail ties and spikes
5. Road Transportation
  - a. Corruption & Bribery

Note that no additional issues were proposed for the following industries.

1. Auto Parts;
2. Car Rental & Leasing; and
3. Marine Transportation.

The standards development team will conduct further research, including analysis of Form 10-K disclosure, and discussion with industry experts to determine materiality of the issues suggested. In some cases, it may result in addition of an angle and relevant metrics to an existing issue or inclusion of a new issue.

## 1. AUTOMOBILES

### a. Issue: Emissions of Volatile Organic Compounds

Emission of VOCs was suggested by David Tulauskas of GM suggested, “Automotive painting and use of adhesives are large sources of VOCs. They are regulated and permits for VOC emissions are required.” This issue was explored briefly prior to IWG, however EFI was not strong.

SASB Standards Development team researched the following topics in order to determine materiality of the issue:

- Have there been any fines, penalties, or lawsuits against companies for exceeding allowed levels of VOCs?
- How do companies usually ‘dispose’ of VOCs? Are they treated before disposal?
- Are workers exposed to VOCs?
- What are innovations in this space? Examples of companies using non-VOC paint and financial impact of such decisions.
- Which sectors are the largest emitters of VOCs? Is automobiles in the top of the list?
- What are the detrimental effects of VOC emissions?

## **Recommendation**

Do not include this issue.

The issue was considered for inclusion in the Air Emissions issue, however additional research supports our initial hypothesis that it is not a material issue. Research suggests that the issue is well-managed by auto manufacturers. In response to a request for further clarification, David responded “I agree with your assessment that this issue is well-managed and having a chance to re-think my comments based on your email, I support your conclusion that VOC emissions are not material for the auto industry.”

## **2. AIRLINES**

### **a. Issue: Community Relations**

A public interest participant commented that the issue of local community impact should be considered a material issue since “For hubs airlines are active, local communities benefit from employment opportunities airlines offer and business opportunities for local enterprises. On the other hand negative impacts include noise and fuel dumps.”

The standards development team looked at both the issues of noise pollution and fuel jettison (or fuel dumping) prior to the IWG and will continue further research of these issues. Major airlines report on both these issues. For example, Emirates reported Noise Efficiency Factor (dBkm<sup>2</sup>/TK) for both takeoff and landing and number of fuel jettison events and amount of fuel jettisoned.

With respect to noise pollution, there are two main factors. First, since the location of airports is not determined by airlines, the only things within an airline’s control are landing and taking off during permissible hours, and flying in a manner to minimize noise. Second, initial research revealed that fines for exceeding noise limits are not very large or chronic. However, to the extent that concerns over noise pollution limits airport expansion or new airport construction, it could become a material issue.

Fuel dumping or fuel jettison is when a pilot dumps excess jet fuel so that the aircraft can land at the maximum safe landing weight. Since jet fuel is costly, this usually happens only before emergency landing. Since jet fuel contains volatile organic compounds, fuel jettison results in air pollution. Further research will be conducted by SASB to determine the extent to which large commercial airlines dump jet fuel and its implication.

**Noise pollution - SASB will conduct further research on the issue in order to determine its materiality to the airlines industry.**

**Fuel jettison - SASB will conduct further research on the issue in order to determine its materiality to the airlines industry.**

## **Recommendation**

Noise pollution - The issue may be included as a watch list issue to the growing nature of the problem and the potential for materiality in the future.

Fuel jettison – The issue may be included as an environmental issue pending further research.

### 3. AIR FREIGHT & LOGISTICS

#### a. Issue: Political Contributions/ Corruption & Bribery

A market participant commented that “with the SEC now considering disclosure of political contributions as a material factor, and big players active in the field (fedex for instance - maybe the group could investigate whether this is a material metric for the industry to report on.” [sic]

**SASB will conduct further research to determine materiality of the issue for the rail industry.**

### 4. RAIL TRANSPORTATION

#### a. Issue: Trafficking

One public interest participant suggested including illicit activities like drug trafficking. The example cited by the respondent regarding illegal drugs found on Union Pacific rail cars. In 2011, a “Nebraska judge Monday threw out more than \$37 million in fines assessed against Union Pacific Corp. over illegal drugs found on trains coming in the country from Mexico.” Based on initial research, the issue is not deemed material to the rail industry.

**SASB will not add this issue to the material issue list due to lack of evidence of interest or financial impact on rail companies.**

#### b. Issue: Supply Chain Management

An IWG survey respondent mentioned, “The overwhelming majority of intermodal terminals in the U.S. are owned by the major freight railways. Some have outsourced the operations of these terminals (e.g. management of handling equipment) to service suppliers. Outsourcing is driven by cost saving opportunities but labour issues in the supply chain can result in ad-hoc problems with service quality. These can result in reputational damage and lower customer satisfaction. They still need to ensure that there are no issues in terms of product damage, loss or theft, or delays in delivery.”

**SASB will conduct further research to determine materiality of the issue for the rail industry.**

#### c. Issue: Waste Management

Riaz Ahmed of TRC Solutions said, “Railroads dispose close to 25 million ties per year; most of them treated by creosote. Disposal of ties remain issue. Use of ties which lengthen their life such borate pretreated ties should reduce tie disposal problems. Also, with lesser amount of creosote in these ties they can be more amenable for use in energy production. One of the railroads noted that they recovered millions of dollars in salvaging rail spikes.”

**SASB will conduct further research to determine materiality of the issue for the rail transportation industry.**

### 5. ROAD TRANSPORTATION

#### a. Issue: Corruption & Bribery

Rodney Irwin of WCSBD commented, “Express Delivery services sell speed of pick-up and delivery of customer packages. When cross border movements of goods there is a risk in many locations for unfair and in cases corruption of facilitation payments being made to custom officials. The WEF Partnering Against Corruption Initiative (PACI) has been focused on this for some years. Examples of litigation has

also been confirmed with Palipina case in 2011.” This comment may be relevant to Air Freight & Logistics industry as well.

**SASB will conduct further research to determine materiality of the issue for the road transportation industry.**



## Appendix I: Draft List of Issues for Public Comment

The following table comprises issues that are likely to be presented for Public Comment on April 17, 2014, based on SASB's review of IWG comments and additional research. Note these issues are not final and are subject to change.

	Automobiles	Auto Parts	Car Rental & Leasing	Airlines
# Issues	9	10	5	3
Environment	GHG Emissions & Energy Management	Energy Management		Air Emissions & Fuel Management
	Waste Management	Waste Management	Waste Management	
		Water Management	Water Management	
Social Capital			Passenger Safety	Passenger Safety
			Transparent Information & Fair Advice	
Human Capital				
	Employee Health, Safety & Well-being	Employee Health, Safety & Well-being		
	Labor Relations	Labor Relations		Labor Relations
Business Model & Innovation	Product Quality & Safety	Product Quality & Safety		
	Fuel Economy & Use-phase Emissions	Product Stewardship	Fleet Fuel Efficiency	
	Product End-of-life	Product End-of-life		
Leadership & Governance		Competitive Behavior		
	Supply Chain Management	Supply Chain Management		
	Dealership Management			

	Air Freight & Logistics	Marine Transportation	Rail Transportation	Road Transportation
# Issues	6	5	6	4
<b>Environment</b>	Air Emissions & Fuel Management	Air Emissions & Fuel Management	Air Emissions & Fuel Management	Air Emissions & Fuel Management
		Ecological Impacts	Ecological Impacts	
<b>Social Capital</b>			Community Relations	
<b>Human Capital</b>				Employee Recruitment & Retention
	Employee Health, Safety & Well-being	Employee Health, Safety & Well-being		Employee Health, Safety & Well-being
	Labor Relations		Labor Relations	
<b>Business Model &amp; Innovation</b>				
<b>Leadership &amp; Governance</b>	Business Ethics & Payments Transparency	Business Ethics & Competitive Behavior		
	Competitive Behavior		Competitive Behavior	
	Accident & Safety Management	Accident & Safety Management	Accident & Safety Management	Accident & Safety Management

## Appendix II: Sample Accounting Metrics

The following table lists the disclosure items (metrics), as they stand currently, for the sustainability topics determined by SASB to be material for the Automobiles industry following IWG feedback. This table provides sample metrics for reference only. The accounting metrics are currently being revised, and final metrics put forward for public comment may be different from the ones outlined below.

Topic	Code	Accounting Metric
<b>Greenhouse Gas Emissions &amp; Energy Management</b>	TR0101-01	Gross global Scope 1 emissions in metric tons CO <sub>2</sub> -e. Breakdown of total emissions by countries with more than 5% of total Scope 1 emissions.
	TR0101-02	Total annual energy consumed (gigajoules); percentage from purchased grid electricity. Percentages of non-grid energy from (a) fossil fuels and (b) renewables (e.g., wind, biomass, solar).
<b>Waste Management</b>	TR0101-03	Amount of total waste (tons) from plant operations, broken down by the following waste types: (1) hazardous; and (2) non-hazardous. For each waste type, indicate the percentage that is recycled, treated, incinerated, and landfilled.  <b>Technical Note:</b> Total waste is defined as by-products from operations that are recycled, treated, incinerated or landfilled.
<b>Employee Health, Safety &amp; Well-being</b>	TR0101-04	Report the following occupational injury statistics, broken down by full-time and contract employees for domestic and foreign operations: <ul style="list-style-type: none"> <li>• Total Recordable Injury Rate (TRIR);</li> <li>• Lost Time Injury Rate (LTIR);</li> <li>• Fatality Rate (excluding illness fatalities);</li> <li>• Near Miss Frequency Rate.</li> </ul> <b>Technical Note:</b> Rate = (statistic count / total hours worked)*200,000
	TR0101-05	Discussion of efforts to assess, monitor, and reduce exposure of employees to human health hazards, including but not limited to, heat, noise, ergonomic strain, mechanical systems and chemicals. Describe management approach to both short-term (acute) and long-term (chronic) health risks.
<b>Labor Relations</b>	TR0101-06	Percentage of active workforce covered under collective bargaining agreements, broken down by U.S. and foreign employees.
	TR0101-07	Number of strikes and lockouts resulting in work stoppages of at least one day, including the number, duration, and reason for the stoppage (in days).
	TR0101-08	Number of retirees and dependents receiving pension benefits, relative to number of active employees.

Topic	Code	Accounting Metric
<b>Product Quality &amp; Safety</b>	TR0101-09	<p>Number of (a) vehicle models offered; and (b) vehicles sold, broken down by Global New Car Assessment Programme (NCAP) safety score for new cars.</p> <p><b>Technical Note:</b> During each fiscal year (FY) there may be multiple model years (MY) sold (e.g., during FY 2013, there were new models from MY 2013 and MY 2014 sold).</p>
	TR0101-10	<p>List of vehicle models recalled; indicate whether voluntary. For each recall, indicate number of vehicles affected, whether the recall is due to faulty product design or faulty production, significant outcomes (e.g., causes of accidents or passenger fatalities), and corrective actions taken.</p> <p><b>Technical Note:</b> The distinction between faulty product design and faulty production is intended to capture whether the product is universally problematic (i.e. an issue of product or component design), or if there was a badly produced batch of product (i.e., an issue of quality control in production).</p>
	TR0101-11	<p>Percent of cars sold that are ranked by Kelley Blue Book's 5-Year Cost to Own as the top 5 best performers within its vehicle class.</p>
<b>Fuel Economy &amp; Use-phase Emissions</b>	TR0101-12	<p>Corporate average fleet efficiency (CAFE); indicate percentage of total vehicles sold (by unit) for each of the following vehicle types: gasoline, diesel, ZEV/PZEV, and alternative fuel (including flex fuel).</p> <p><b>Technical Note:</b> CAFE standards reflect the sales-weighted average fuel economy, expressed in miles per gallon, of a manufacturer's fleet of passenger vehicles with a gross weight of 8,500 lbs. or less. This calculation uses a harmonic mean of vehicle fuel efficiency (i.e. the reciprocal of the average of the reciprocals).</p> <p>ZEV = Zero Emission Vehicles include ultra-low emitting plug-in electric hybrid vehicles (PHEV) along with non-polluting fully electric cars and fuel cell vehicles.</p> <p>PZEV = Partial Zero Emission Vehicles meet ARB's Super Ultra-Low Emissions standard of 0.03 grams per mile of non-methane organic gases and nitrogen oxides, have no evaporative emissions, and have a 15 year/150,000 mile warranty.</p>
<b>Product End-of-life</b>	TR0101-13	<p>Sales-weighted percentage of materials in fleet (by weight) that are (a) recyclable; and (b) recoverable.</p> <p><b>Technical Note:</b> Recyclable is defined as able to be reprocessed for the original purpose or for other purposes, but excluding energy recovery. Energy recovery means the use of combustible waste as a means to generate energy through direct incineration with or without other waste, but with recovery of the heat. This definition is consistent with the EU End of Life Vehicle Directive.</p> <p>Recoverable is defined as able to be salvaged for further use, including use as a fuel or other means to generate energy, consistent with the EU End of Life Vehicle Directive (Annex IIB to Directive 75/442/EEC).</p>

Topic	Code	Accounting Metric
	TR0101-14	<p>Describe approach to optimizing the recycling and recovery rates; include discussion of management approach to recovery of mercury, tires, e-waste, and batteries. For markets with mandatory vehicle take-back programs, number of vehicles recovered through take-back programs; percentage (by weight) that are:</p> <p>(a) reused &amp; recycled;</p> <p>(b) recovered, but not recycled, consistent with Annex IIB to Directive 75/442/EEC; and</p> <p>(c) landfilled or otherwise disposed consistent with Annex IIA to Directive 75/442/EEC.</p> <p><b>Technical Note:</b> Among others, the EU, Japan, and Korea have mandatory vehicle take-back requirements.</p> <p>Consistent with the EU End of Life Vehicle Directive (Directive 75/442/EEC):</p> <ul style="list-style-type: none"> <li>• "Reuse" means any operation by which components of end-of life vehicles are used for the same purpose for which they were conceived;</li> <li>• "Recycling" means the reprocessing in a production process of the waste materials for the original purpose or for other purposes, but excluding energy recovery. Energy recovery means the use of combustible waste as a means to generate energy through direct incineration with or without other waste, but with recovery of the heat;</li> <li>• "Recovery" means any of the applicable operations provided for in Annex IIB to Directive 75/442/EEC, including use as a fuel or other means to generate energy; and</li> <li>• "Disposal" means any of the applicable operations provided for in Annex IIA to Directive 75/442/EEC.</li> </ul>
<b>Supply Chain Management</b>	TR0101-15	Discuss existing or projected constraints with obtaining components (or raw materials), including those related to political situations, local labor conditions, natural disasters, climate change, geography, regulations, or restricted/limited availability. Discuss any production shortfall resulting from materials supply; indicate the cause and the relative impact on production.
	TR0101-16	Percentage of Tier I suppliers in full compliance with the registrant's environmental and social/labor requirements.
	TR0101-17	Discuss the process for managing environmental, social, and quality control risks within the supply chain including screening, codes of conduct, audits, and certifications. Indicate if audits are first party, second party, or third party.
<b>Dealership Management</b>	TR0101-18	Total vehicle sales (on a unit basis) to customers in the following bands of credit scores: High (>700), Medium (581-699), and Low (<580). For each credit tier, indicate median discretionary interest rate mark-up (as a percent), for all borrowers, for women, and for minorities. Discuss policy on discretionary mark-ups by dealers, including any limits set by the manufacturer.
	TR0101-19	Description of management approach to minimize risk of anti-competitive practices due to exclusive dealer territories established through contractual agreements with franchisees or government protections.



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