Aligning ESG with Commercial Growth

Midwest M&A / Private Equity Conference

May 5, 2022

Columbus, Ohio

What is ESG?

Doing business in a way that considers environmental, social & governance elements

Top of mind for boards, investors, customers, employees, suppliers, and regulators

Philosophy that social & environmental issues should be of equal concern as profits

Increasing scrutiny, activism

Environmental

- **Climate change, waste, water, chemicals, emissions, biodiversity**

Social

- **Modern-day slavery, safety, diversity, working conditions, environmental justice, fair access to healthcare**

Governance

- **Board diversity, climate competency, executive compensation, lobbying & political contributions**

A Crowded Disclosure Landscape

MULTIPLE **ORGANIZATIONS**

Value Reporting Foundation / TCFD / CDSB / GRI / Bloomberg / MSCI / CDP / TruValue Labs / RepRisk / Sustainalytics / Refinitiv / DJSI / FTSE4Good

FIT IN 4 DISTINCT GROUPS:

1 Publish guidance for voluntary disclosure, often with company feedback loops

2 Request data from companies via questionnaires

3 Aggregate publicly-available data from companies

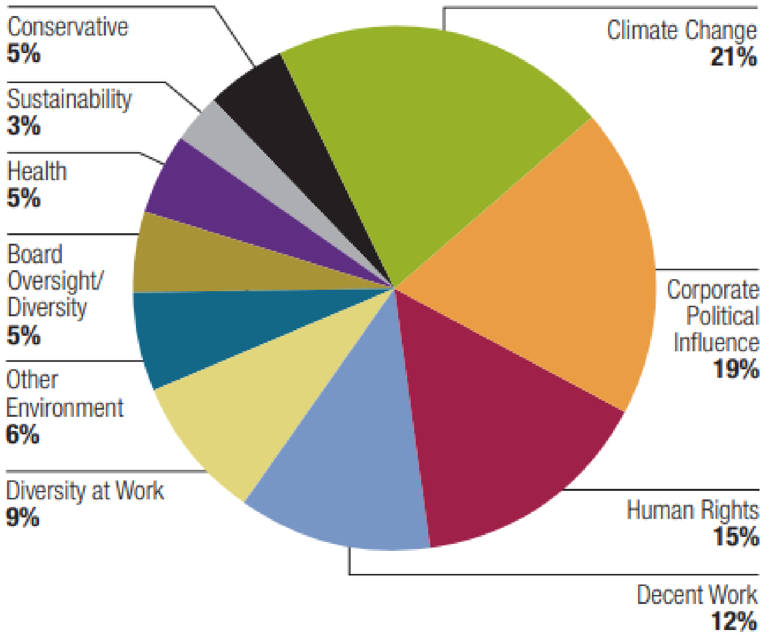
4 Create assessments of companies based on public and/or private information to sell to investors

Source: Value Reporting Foundation

ESG-Related Activism On The Rise

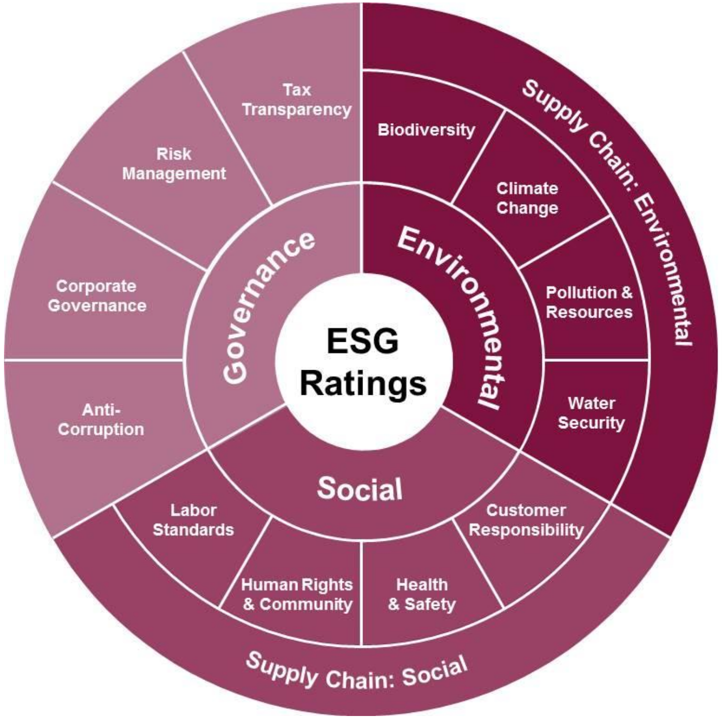
- Record 529 ESG shareholder resolutions filed – up 22%
- Climate issues top the agenda at 110 proposals
  - Near total focus on GHG emissions and transition plans
- +20 shareholder proposals filed with 14 electric utilities
  - 1/3 focus on diversity, equity and inclusion

2022 Shareholder Proposals



Source: proxypreview

Disclosure is Challenging



- Frameworks, standards, ratings, rankings
- Fast-changing ESG landscape – globally
- Goalpost keeps moving, bar getting higher
- Activism increasing
- SEC climate disclosure rule sets the stage

AMERICAN ELECTRIC POWER
BOUNDLESS ENERGY™

2022 ESG/Sustainability Trends

More pressure to link executive comp to ESG performance

Companies will adapt technology to bridge the digital divide

Growing scrutiny of net-zero carbon goals – transition plan

Corporate purpose will be important to engaging, retaining employees

Workplace flexibility, worktime will change how companies operate

ESG Trends to Watch

Corporate Purpose
Climate Transition Plan
Just Transition/Climate Justice
Human Capital Management
ESG Regulation
Stakeholder Capitalism
Supply Chain Resilience

Enhanced human capital management disclosures

Better insights into DEI practices at all levels

Growing focus on supplier diversity

Greater supply chain transparency & tools to manage risk

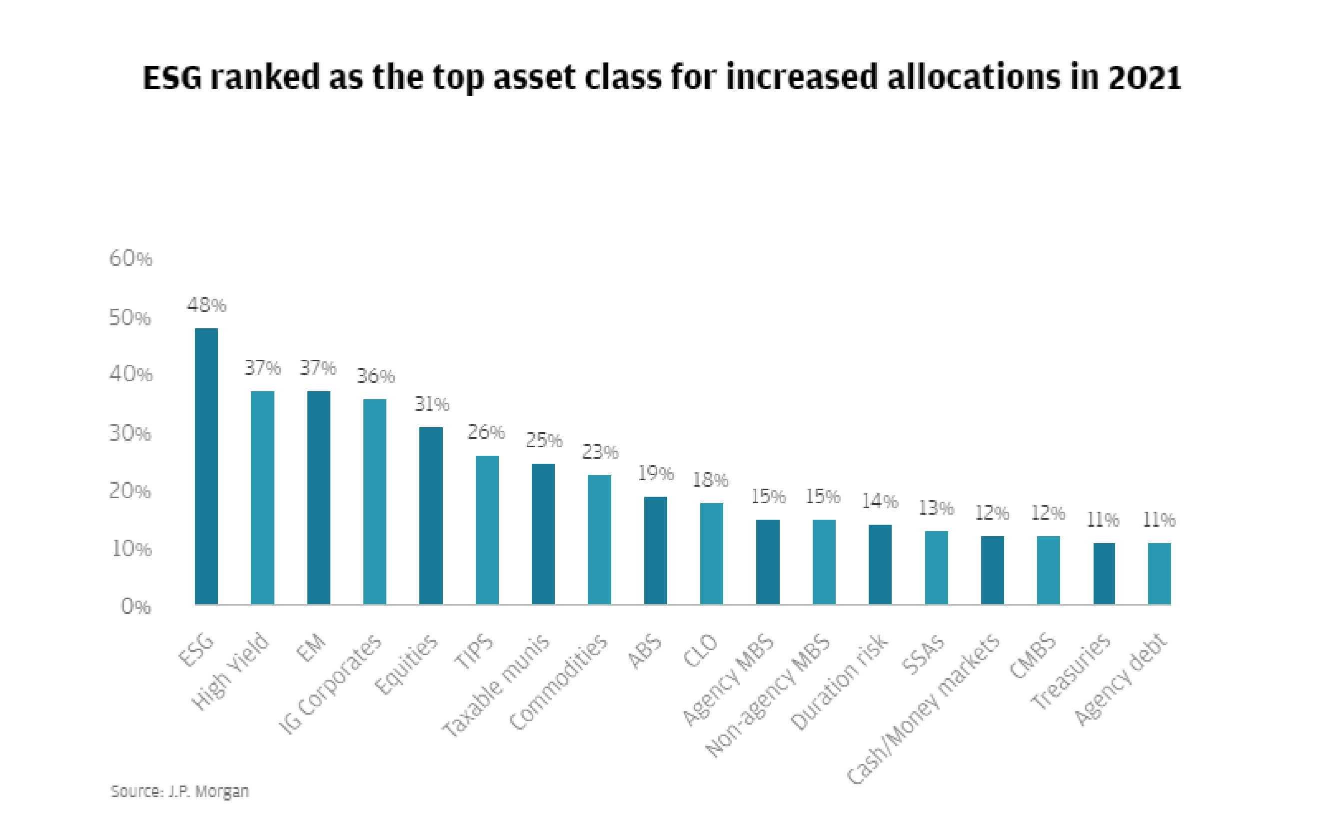
Leverage economic influence to demand action on social issues employees, customers care about

Source: SustainAbility Institute at ERM

Drivers of ESG in M&A and PE

- Investors are increasingly focusing on ESG
  - BlackRock's Annual CEO Letter
- Investors and potential acquirers are evaluating a company's ESG strategy as part of their value
- Impact investing and ESG Funds
- United Nations Principles for Responsible Investment (UN PRI)

ESG Investing by the Numbers

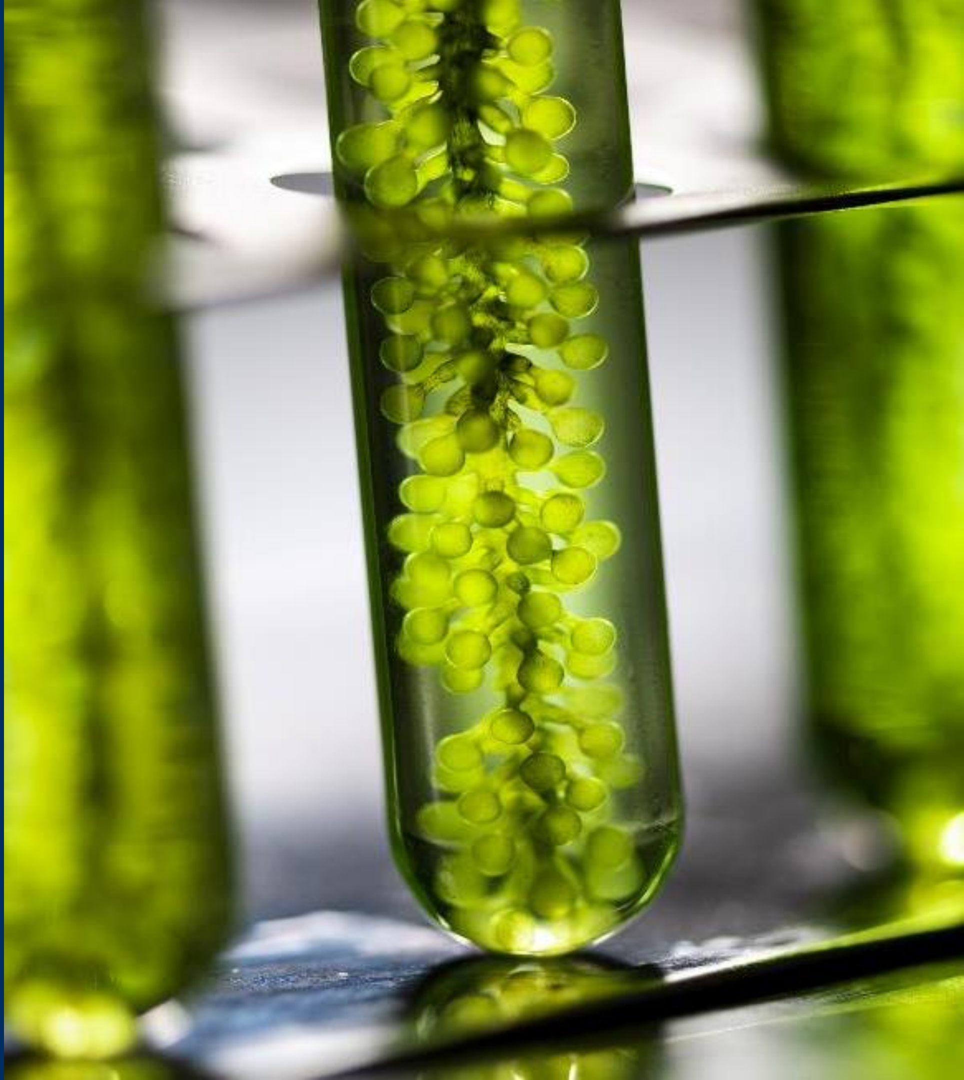


Benefits of ESG for PE and M&A

- Manage Risk
- Value Creation
- Market Differentiator
- Future Proof Business

For Consideration

- **Who are your stakeholders and what do they care about? How can you deliver to their expectations?**
- **What are the ESG topics that are material to your business?**
- **Do you have an ESG Strategy?**
- **What about a roadmap and implementation plan?**
- **ESG Due Diligence is key to understanding risks and effective integration of M&A**
  - **Make sure that you have the data to back-up your claims!**



Example Portfolio Company ESG Activities

PRE-CLOSE

ESG Due Diligence & Integration Planning:

Inputs: Utilize SASB, GRI & other evaluation standards depending on PEG philosophy and investment thesis

Outputs: Buildout of an ESG Profile with emerging risks and opportunities identified

HOLD PERIOD

ESG Roadmap:

Inputs: DD findings, observations from business leaders & Gap Framework assessment

Outputs: Prioritized recommendations and implementation guidance based on benefit and maturity

ESG Strategy Execution (many elements):

Inputs: ESG Roadmap project plan

Outputs: Service execution across 3 major dimensions: Environmental, Social & Governance

EXIT

Sell-side CIM, roadmap strategy and DD prep support can provide enhanced value at exit

SEC Proposed Rule on Climate-Related Disclosures

"Today, investors representing literally tens of trillions of dollars support climate-related disclosures because they recognize that climate risks can pose significant financial risks to companies, and investors need reliable information about climate risks to make informed investment decisions."

SEC Chair Gary Gensler

March 21, 2022

- Released March 21, 2022
- Comment period open though May 20, 2022

Proposed Disclosures

- ***Financial statement footnote disclosures:***
  - Impact on financial statement line items related to **severe weather events and other natural conditions** and transition activities if **more than 1%** of the related line item.
  - Expenditures related to **mitigating the risk of severe weather events** and other natural conditions and transition activities **if more than 1%** of the total amount expensed or capitalized.
  - How severe weather events and other natural conditions and transition activities affected estimates and assumptions are reflected in the financial statements.
- ***GHG emission disclosures:***
  - **Scope 1 and Scope 2 GHG emissions** separately disclosed on a disaggregated (by each GHG) and aggregated basis.
  - **Scope 3 GHG emissions** in gross terms, if the company has set a GHG emissions **target or goal** that includes Scope 3 emissions or if Scope 3 emissions are **material**.
- ***Qualitative disclosures:***
  - Prospective risks and material impacts on company's "strategy, business model, and outlook" caused by climate change over the short-, medium- and long-term.
  - The **processes for detecting, evaluating, and managing climate-related risks** and whether those processes are integrated into the company's broader risk management program.
  - Any **internal carbon price**, the registrant's internal carbon price and how such price is determined.
  - Any **scenario analysis** to assess its business in the context of climate-related risks, a description of the scenarios, assumptions, and projected financial impacts.
  - Any climate **transition plans**, a description of such plan as well as relevant targets and metrics.

Goals, Oversight and Timing

Publicly Disclosed Goals

Scope, timing and interim targets.

Plans for how goals will be achieved.

Annual update of progress toward the targets or goals and how such progress has been achieved.

Information about carbon offsets or renewable energy certificates (RECs), including how much of the progress made is attributable to offsets or RECs, if they are part of the company's climate-related targets or goals plan.

Board Oversight

Provide detailed governance disclosures

Detail Board and management **oversight** of climate-related risks, the risk management process, and the company's response.

Detail the climate related **experience** of Board, management or ESG committee

How & When

Include the disclosures in company's registration statements as well as **annual reports**.

The disclosures outlined in the **financial statement footnote disclosures** would be required in the financial statements.

Form 10-K would include other disclosures, including GHG emissions, immediately before MD&A.

Timing: The disclosures would be due at the same time as the company's annual report.

Emissions Disclosures

Scope 1 & 2

- Scope 1: **direct GHG emissions** from sources that are controlled or owned by the company
- Scope 2: **indirect GHG emissions** from upstream and downstream activities
- Required on a gross basis (before consideration of any offsets) and relative to intensity, if company set a GHG emissions target or goal that includes Scope 3 emissions or if Scope 3 emissions are material.
- *Note:*
  - Required FY 2024 (filed in 2025)
  - Independent audit not required
  - Provides safe harbor for for liability from Scope 3 emissions disclosure

Scope 3

- GHG emissions not within company's Scope 1 or 2, but result from activities and assets not owned or controlled by the company, but **that the company indirectly impacts in its value chain**
- Separately disclosed on a disaggregated (by each GHG) and aggregated basis.
- Required on a gross basis (before consideration of any offsets) and relative to intensity (e.g., tons of carbon dioxide per dollar of revenue).
- *Note:*

  Required FY 2023 (filed in 2024)

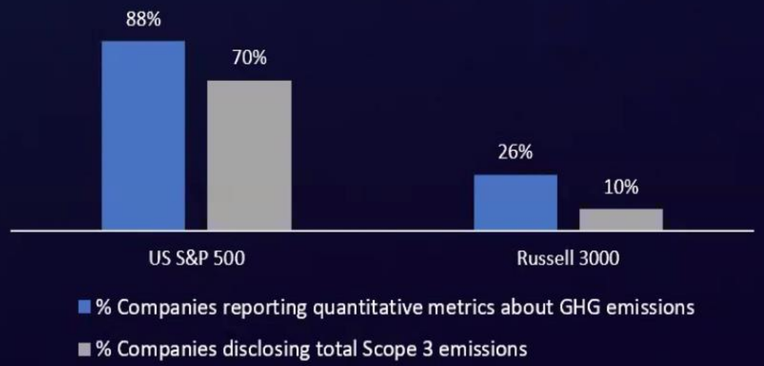
  Audited with "limited assurance" for FY 2024

  Audited "reasonable assurance" for FY 2026

GHG Protocol: List of scope 3 categories[1]

Upstream or Downstream	Scope 3 Category
Upstream Scope 3 Emissions	1. Purchased goods and services 2. Capital Goods 3. Fuel- and energy-related activities (not included in scope 1 or scope 2) 4. Upstream Transportation and distribution 5. Waste generated in operations 6. Business travel 7. Employee commuting 8. Upstream leased assets
Downstream Scope 3 Emissions	9. Downstream transportation and distribution 10. Processing of sold products 11. Use of sold products 12. End-of-life treatment of sold products 13. Downstream leased assets 14. Franchises 15. Investments

Carbon Emissions Reporting at U.S. Companies by Index[2]



ISS CORPORATE SOLUTIONS

1 Source: GHG Protocol

2 Source: ISS QualityScore Data as of April 13, 2022

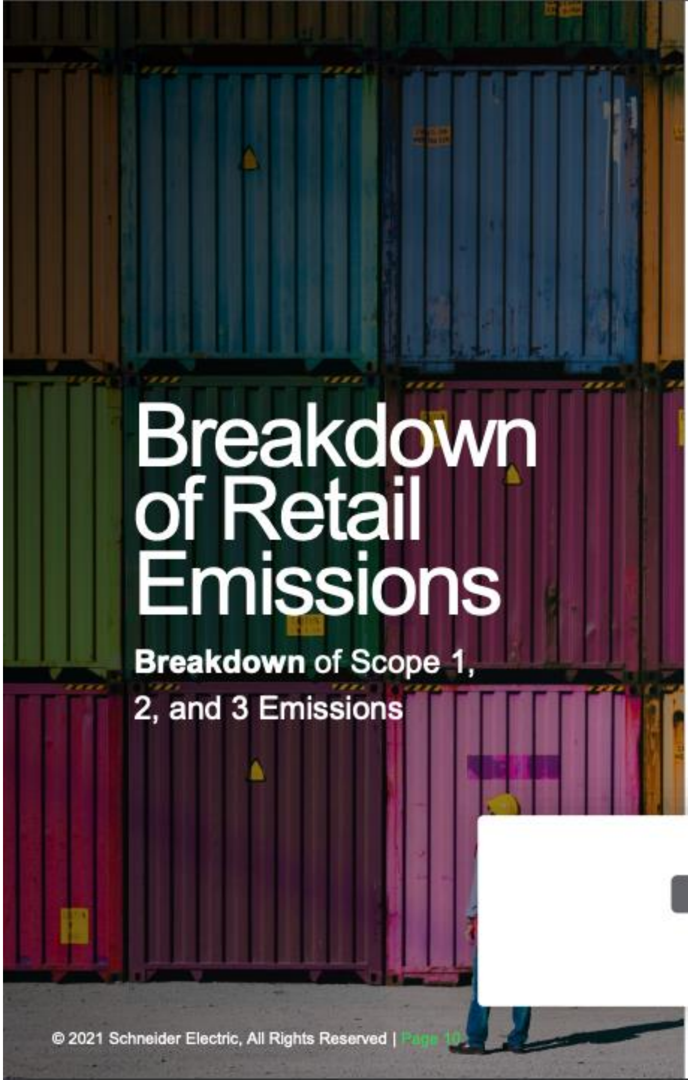
Assuming the proposed rules are adopted with an effective date of Dec 2022, and the filer has a fiscal year ending Dec 31:

SEC's Proposed Mandatory Reporting Timeline

Registrant Type	Disclosure Compliance Date	
	All proposed disclosures, including GHG emissions metrics: Scope 1, Scope 2, and associated intensity metric, but excluding Scope 3	GHG emissions metrics: Scope 3 and associated intensity metric
Large Accelerated Filer	Fiscal year 2023 (filed in 2024)	Fiscal year 2024 (filed in 2025)
Accelerated Filer and Non-Accelerated Filer	Fiscal year 2024 (filed in 2025)	Fiscal year 2025 (filed in 2026)
SRC	Fiscal year 2025 (filed in 2026)	Exempted

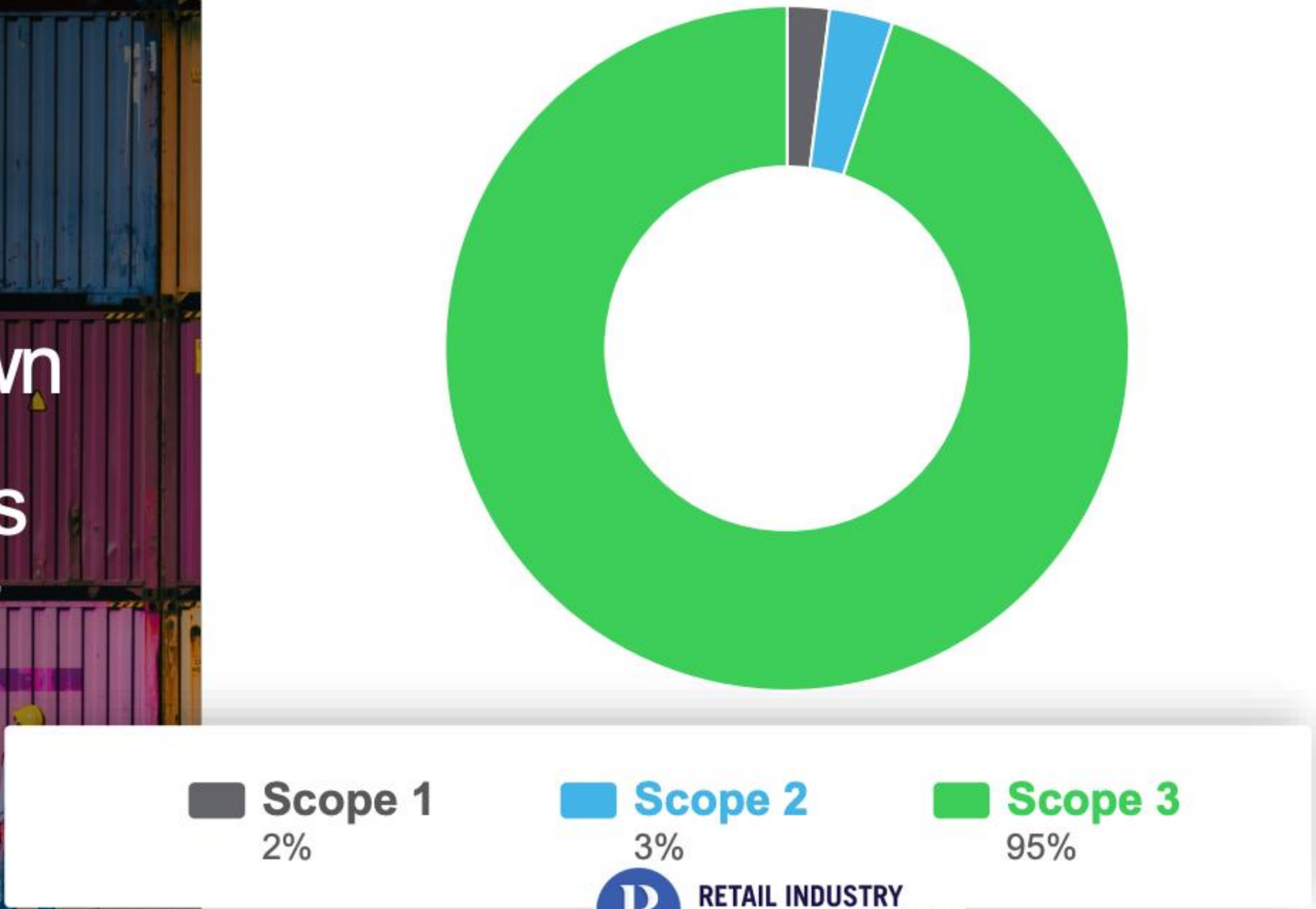
Filer Type	Scopes 1 and 2 GHG Disclosure Compliance Date	Limited Assurance	Reasonable Assurance
Large Accelerated Filer	Fiscal year 2023 (filed in 2024)	Fiscal year 2024 (filed in 2025)	Fiscal year 2026 (filed in 2027)
Accelerated Filer	Fiscal year 2024 (filed in 2025)	Fiscal year 2025 (filed in 2026)	Fiscal year 2027 (filed in 2028)

See https://www.sec.gov/files/33-11042-fact-sheet.pdf



Breakdown of Retail Emissions

Breakdown of Scope 1, 2, and 3 Emissions

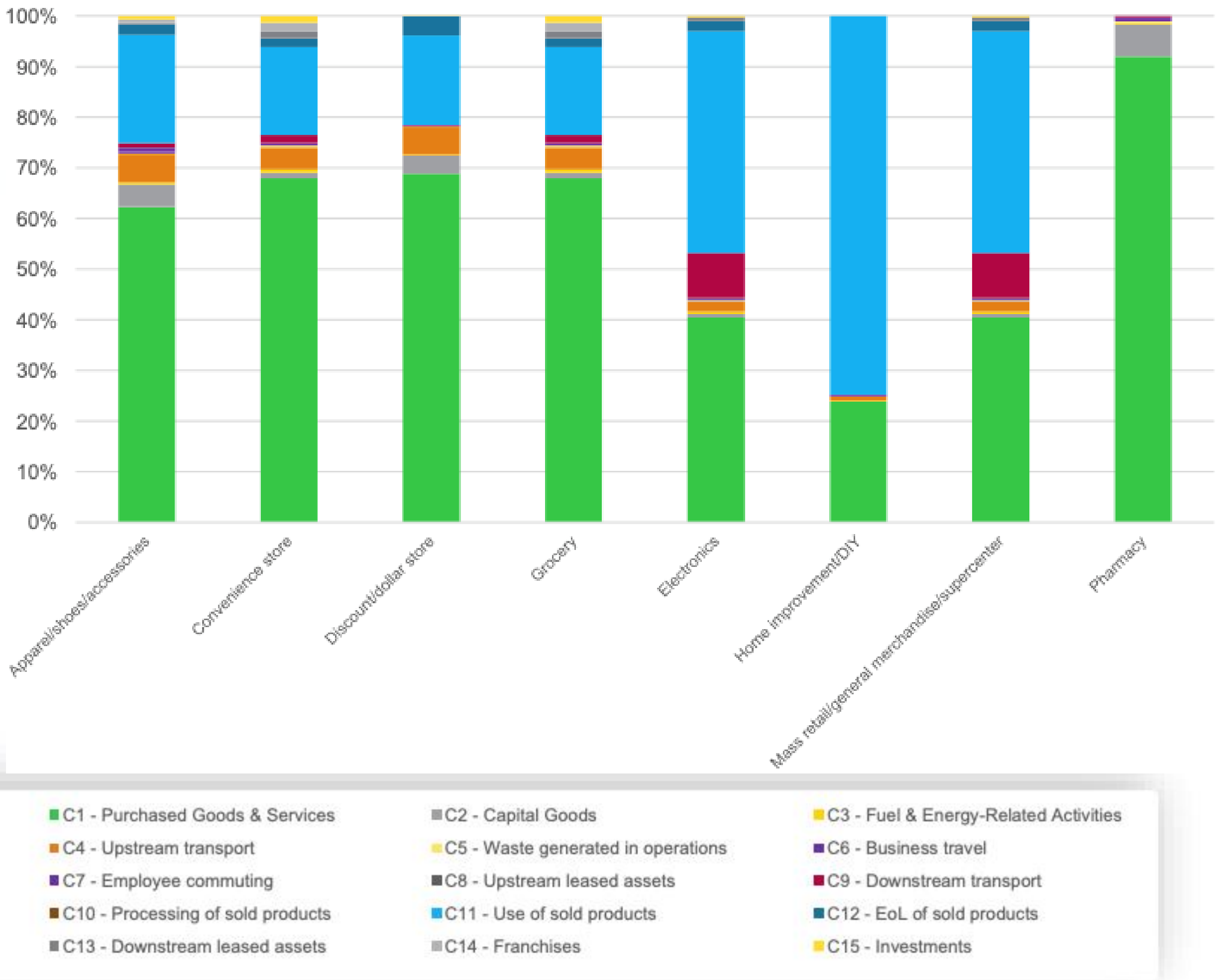


RETAIL INDUSTRY LEADERS ASSOCIATION

Breakdown of Retail Emissions

Breakdown of

Scope 3 Categories



***Calculated from scope 3 reporting to 2020 CDP Climate Change Questionnaires from retailers with an approved Science-Based Target (except Home Improvement/DIY, which used 2020 CDP Climate Change Questionnaire reporting from The Home Depot & Loewe's Companies.)*

Contact Us

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